MARKETIZATION AND YUANIZATION: ECONOMIC CHANGES IN THE DPRK

Christopher Green
University of Cambridge

Introduction

Implemented without prior warning on November 30, 2009, the DPRK currency redenomination confirmed something that had been increasingly apparent since 2002: that one of the most pressing issues facing the mass of DPRK citizens in the modern era is ensuring access to sources of value in which to securely store their assets. This is a crucial issue not only because inflationary pressures are putting the North Korean won under constant strain; it is also the case because the government of the DPRK has demonstrated an apparent readiness when necessary to expropriate the assets of the majority for the benefit of a minority, making economic policy an issue of class struggle rather than fiscal rebalancing.[1]

Policies of the type exemplified by the currency redenomination are not without global precedent; history is littered with economic policies that had serious ramifications for specific groups in the target society. One example, the December 1979 "demonetization" of Zaire, is described at length in this essay. In countries like the DPRK (and Zaire), which are typified by undemocratic systems of governance, non-existent property rights, banking systems wholly subordinate to official fiat, and state ambivalence or hostility to free markets, such policies are a particularly acute threat to human security, as they leave citizens at risk of livelihood shocks and with a circumscribed choice of value storage mediums.

Some of the DPRK government's tools of expropriation are impossible to restrict: the extraction of non-tax payments from the civilian by a state representative of one sort or another, for example. But in other areas civilians are able to insulate themselves. One way in which they can do so is to store their liquid

1 The *Daily NK* provides North Korean Won-US Dollar exchange rate data: http://www.dailynk.com/korean/market.php [in Korean].

assets in foreign currency, and this is an increasingly popular choice. Although other currencies are also used for the same purpose, the prevalence of the phenomenon in towns and cities along the border with China has led me to label the process *Yuanization*.

State Forfeits Control of Livelihoods

In order to understand the critical importance of *Yuanization*, it is necessary to look back into the history of DPRK marketization itself. For the purpose of this article, that history is taken to begin in 1994 and continue through the present day. It should be noted, however, that small farmers' markets and a handful of other low-impact private commercial activities have actually existed in some form or another throughout much of the DPRK's 60-year history.[2]

Nevertheless, widespread market activities only firmly took hold in the mid-1990s. This was due to the creation of a space, both political and physical, into which private commerce could be inserted. The most commonly cited catalysts for this process of governmental regression and simultaneous space creation were the collapse of the Soviet Union in 1990-91 and the death of national founder Kim Il-sung on July 8, 1994. These are also generally seen as the primary causes of a famine that killed anywhere from 600,000 to three million people over the course of three to five years, mostly, but far from exclusively, in the rural north of the country (Jagang, Ryanggang and Hamgyeong provinces).[3,4]

This history must be put into broader context, however. High-level sources demonstrate that the DPRK leadership was aware that their command economic model was failing much earlier than this. Most notably, former Korean Workers' Party International Secretary Hwang Jang-yop notes in his 1998 memoirs, "I didn't have all that much interest in statistics, but it was impossible not to notice that the North Korean economy was constantly recording minus figures."[5]

"It was no coincidence," Hwang goes on to say, "that the time when Kim Jong-il came to power and the time when the North Korean economy went into decline occurred simultaneously." Kim assumed a critical mass of political power in September 1973 when he took over the party departments in control of personnel and propaganda via the seventh plenary session of the Fifth Central Committee of the Workers' Party, and was certainly in unassailable control by

---

2 Hak-sun Baek, *Bukhan gwonnyeokui yeoksa* (The history of power in North Korea), (Seoul: Hanul Books, 2011).

3 Baek, *Bukhan gwonnyeokui yeoksa*.

4 Ministry of Unification, *Bukhan ihae 2011* (North Korea 2011), (Seoul: Ministry of Unification, 2011).

5 Jang-yop Hwang, *Naneun yeoksaui jinnireul boatda* (I saw the truth of history) (Seoul: Zeitgeist, 1998), 276.

the time of the Sixth Workers' Party Congress in 1980.[6] Therefore, Hwang's claim is that Kim Jong-il knew in the 1970s that the DPRK economy was faltering badly. Hwang also records that "after 1986" the situation began to take an even more desperate turn, another data point that falls years prior to either the death of Kim Il-sung or the collapse of the USSR.[7]

However, no economic policy of significance was implemented by the government of Kim Il-sung or Kim Jong-il in response to this state of affairs, or to clear reform signals emanating from Beijing and Moscow. This implies, at best, that political stability was seen as more important than economic development. As a result, by the time events on the ground had begun to reach a head in 1994-1995, millions of people had already stopped receiving the rations that had hitherto met their minimum daily needs under the state-run Public Distribution System. According to refugee interviews cited by Marcus Noland and Stephan Haggard in *Witness to Transformation*, state distribution had by and large ceased to provide for most people by 1993.[8]

In response, citizens adopted a range of coping strategies. These included compressed household consumption; direct, unofficial barter between individuals and entities; foraging on hills and mountainsides; defection; and soliciting remittances from relatively more affluent family members.[9] Moreover, many people also entered the rapidly developing unofficial economy. Mr. Lee is one such person; a study in what coping with famine conditions through the unofficial economy meant in practice. A resident of Hyesan, the largest city in northerly Ryanggang Province, his career remained on an unremarkable trajectory through the 1980s and into the 1990s. This meant graduating from high school and entering the military. There he rose through the ranks, and upon being discharged, went to and subsequently graduated from the Korean Workers' Party college. At that time, a party card was a guarantee of the desirable benefits that only accrued to officials. A newly minted party cadre, Mr. Lee soon found himself dispatched to oversee the work of a public utility in Hyesan.

However, the Public Distribution System had already begun to show signs of faltering badly, and events soon started to spiral out of control. Over a relatively brief period of months, Mr. Lee found himself isolated: the manager of 28 workers but without the support of a rationing system through which to meet

6 Ministry of Unification, *Bukhan ihae 2011*, 51.

7 Sung-chull Kim, *DPRK under Kim Jong Il: From Consolidation to Systemic Dissonance* (Albany, NY: State University of New York Press, 1996).

8 Stephan Haggard and Marcus Noland, *Witness to Transformation: Refugee Insights into North Korea* (Washington, DC: Peterson Institute for International Economics, 2011).

9 Ibid.

their daily needs. Therefore, knowing that many of the medicinal herbs growing wild in hilly northern areas of the DPRK were popular in China, he organized his men to abandon their work and gather them. In the dead of night he would then float bags of the herbs across the Tumen River on an inner tube, and a Chinese partner on the other side would float back bags of wheat flour. By distributing this bartered income among his subordinates and their families, Mr. Lee and his team survived the so-called "Arduous March."[10]

For the sake of brevity, I will not add further description of the way the unofficial marketization phenomenon moved forward in the post-famine era. Suffice to say that markets took firm root thanks to the hard work of individuals, trading entities and loose coalitions, who created a system of not only markets but also transport and logistics. The resultant system came to supply an overwhelming majority of the food and other necessities that helped 95 percent of civilians survive the complete loss of state support.[11]

Pyongyang Bounces Back

While the state forfeited much of its control over the livelihoods of the population during the famine, it never ceded its ruling legitimacy as defined by the right to promulgate legislation. Thus, the administrative apparatus survived, and by around 2000 had recovered sufficiently to try and wrestle back control of the marketization phenomenon.

While constitutional amendments made in 1998 can be said to mark the opening gambit in this plan to return to preeminence, it is the *Economic Management Improvement Measure* of July 1, 2002 that was the greatest and best known. Under the measure, existing markets were legalized, and prices and wages elevated dramatically in what is widely described as an attempt to better reflect costs of production; modest autonomy was also subsequently granted to enterprises, and a debate is said have begun as to how far the liberalization movement should be allowed to go.[12]

However, there was another element to the changes when seen from the ground. This was a confiscatory element, one that directly targeted those indi-

---

10 Mr. Lee gave testimony to this effect at a conference organized by the US Institute of Peace (USIP) in Washington, DC, in October 2010.

11 Haggard and Noland, Witness to Transformation. Evidence from South Korean intelligence sources suggest that there are still approximately 2.5 million DPRK citizens in "strategic sectors" that receive reliable rations from the state. However, this is done through a completely different ration system to the PDS, one that uses alternative funding sources (source withheld).

12 Robert Carlin and Joel Wit, "The debate in bloom" in *The Adelphi Papers* 46, no. 382 (2006): 35-52; and Bernhard Seliger, "The July 2002 Reforms in DPRK: Leiberman-Style Reforms or Road to Transformation?" *North Korean Review* (2005): 22-37.

viduals who had accumulated capital during the famine. This was because by raising prices and wages dramatically, without warning and without countermeasures to support losses incurred, the policy automatically and unavoidably eroded the value of liquid assets. This, then, was seen by holders of such assets as a confiscatory attack on their livelihoods. It also marked the birth of Yuanization: the time when those few persons who held domestic currency in significant quantities were first shown evidence that their nascent middle class status was at risk of expropriation or devaluation by the forces of state.

Any debate about the true intent of the DPRK government in making these economic changes remains fierce, but is ultimately irrelevant. *It was what it was,* and those few people with money lost much of it. Ms. Jang, a female refugee from Wonsan in Gangwon Province, and someone who, like Mr. Lee, had parlayed a military career into fiscal stability during and after the famine era, put it this way, "People around me learned right then in 2002 that you had to have foreign currency to be safe."

Five Days of Pain: Mobutu's Zaire in 1979

Debate over the intent behind the 2009 currency redenomination continues to this day. Either it was an honest but foolhardy and extremely unsophisticated attempt to rein in inflation, or a full frontal assault on the market economy. A few, drawing the link between 2002 and 2009 extremely tight, believe that the currency redenomination had actually been planned since 2002, and cite the dates of production on some of the new currency as evidence of this.[13]

The details of the policy are not subject to debate, however. It began without prior warning on the morning of November 30, 2009. Under it, the North Korean won was exchanged at a rate of 100:1, but with a limit on per person exchanges. Initially this limit was set at 100,000 won, but was later raised to 150,000 won following public protest. Families could exchange a certain sum per family member, while a further 300,000 won could also be exchanged, but only if it was put into a state-run bank. The state was to announce new prices for goods, and the entire exchange process had to be completed within seven days.

In line with the "inflation control" hypothesis, one official from the DPRK central bank told the pro-DPRK newspaper *Choson Sinbo* some days after the redenomination took place that it had been done because inflation was undermining the state's policy to cope with natural disasters and the collapse of the

13 Gwang-min Jung, "Currency Reforms: Rationales and Reasons," *Daily NK,* December 17, 2009, http://www.dailynk.com/english/read.php?cataId=nk01100&num=5789.

Soviet Union. Under such an interpretation, the currency reform was a key plank in efforts to right the listing North Korean economic ship.[14]

However, as in the case of 2002, the appearance of the policy to people on the ground was one of outright expropriation of assets by the state, supporting the second view: namely, that Pyongyang intended to undermine, rather than improve, the market economic system. This perspective was shared by some international observers, among them economist Marcus Noland and political scientist Stephan Haggard, who wrote in a policy brief in January 2010:

> Confiscatory currency reforms are a form of asset redistribution, or more accurately, asset levelling. Such conversions either tax those with excess cash balances (if they can be deposited in bank accounts on unfavourable terms and subsequently withdrawn) or destroy 'excess' cash wealth altogether. In the North Korean case, this last motive appears central: Currency reform was designed to target groups engaged in market activities that not only generate cash earnings but also require cash balances given the underdevelopment of the North Korean financial system, while at the same time providing compensatory allocations to favoured groups closely connected to the state.[15]

If, as Haggard and Noland claim, the redenomination was a tool used to wipe out private wealth held by certain groups, it has strong parallels with the "demonetization" policy of the government of Zaire. Implemented in December 1979 and led by another authoritarian dictator in the shape of President Mobutu Sese Seko, demonetization also had a time limit and strict limits on amounts that could be exchanged.

In the Zairian case the time limit was five days, though a number of these were weekend days on which banks, the location for all exchanges, were to be closed. Due to the geography, poverty, poor infrastructure and largely rural population of Zaire, this was tantamount to a guarantee that many citizens could not reach a bank in time to exchange their assets.[16] Again, just as in North Korea, there were also strict limits on amounts of old currency that could be exchanged

---

14 I-ruk Kang, "'Currency Exchange Measure: Purpose Is to Protect Working People's Interests, to Stabilize, Improve Their Living'—We Hear From Cho Seong-hyeon, Senior Staff Member of the Central Bank—'Material Ground Laid for Fighting Off Inflation,'" *Choson Sinbo*, December 4, 2009 [in Korean].

15 Stephen Haggard and Marcus Noland, "The Winter of Their Discontent; Pyongyang Attacks the Market," PIE Policy Brief PB10-1 (2010).

16 Crawford Young and Thomas Turner, *The Rise and Decline of the Zairian State* (Madison, WI: University of Wisconsin Press, 1985).

for new. Individual citizens were allowed to exchange just 3,000 units of the old currency. Small businesses were allowed to exchange 5,000 units, while larger companies were limited to 20,000 units. In a statement that echoes that carried by *Choson Sinbo*, President Mobutu subsequently indicated that his government had intended the policy to encourage people to use banks, and that through it the Zairian authorities had hoped to rein in inflation and create a stronger currency by recovering sums stored by speculators in the unofficial economy.[17]

However, a number of anecdotes from the era support the belief of Janet MacGaffey and others that the policy was not driven by these motivations. Most notably, there was the case of a number of cooperatives organized to overcome credit difficulties: despite a membership said to be around 32,000 and funds totalling more than 5 million units of old currency, the Zairian central bank branded these entities illegal and refused to allow them to change any money at all. At the other end of the spectrum, it is estimated that state employees in banks and other privileged positions appropriated between 20 percent and 40 percent of the total new money supply. In the words of Dr. Emizet Kisangani:

> The big winners were bank managers and high-ranking officials who had no limit in exchanging their banknotes to new ones. The losers were the majority of farmers who lost their life savings, usually kept in pillows, mattresses or jars.[18]

Of course, it remains possible that President Mobutu was speaking honestly when he said he had desired to strengthen the banking system through the demonetization. However, even if this were in fact true, intent would still be far less pertinent than on-the-ground reality. Thus, in Zaire as in the DPRK, in demonetization as in redenomination, all resulted in the de facto expropriation of a nascent trading middle class. For those thus attacked, one inevitable response was to move toward storing value in a foreign currency that could not easily fall prey to the vagaries of state economic policy.

Yuanization: An Inevitable Response to a Man-made Problem

For the broad mass of DPRK citizens who were living hand to mouth in 2002 the message may have been indistinct, but by 2009, when economic conditions had improved somewhat and more people had small amounts of savings, it

---

17 Janet MacGaffey, *Entrepreneurs and Parasites,* (Cambridge: Cambridge University Press, 1987).

18 Emizet Kisangani, "Confronting Leaders at the Apex of the State: The Growth of the Unofficial Economy in Congo," *African Studies Review* (1998): 99-137.

was impossible to ignore. Through the redenomination, the DPRK government, whether wittingly or not, incited movement toward the holding of foreign currency.

My research reveals that a majority of market transactions in most parts of the DPRK now involve foreign currency on some level. I spoke personally with one civilian who recently made a video of market transactions taking place in Chinese currency in Hyesan, and learned that 90 percent of today's market transactions in that city employ foreign currency. Meanwhile, the figure has been put at 80 percent in Hoeryeong, a border city further along the border in North Hamgyeong Province, and as much as 60 percent in port cities further from the Sino-North Korean border such as Nampo and Wonsan.[19]

The key to this is a network of nodes: individuals, many of Chinese-Korean ancestry, whose sole business is exchanging currency. Indicative of the interrelation of the nominally official and unofficial economies, these people are politically well connected, and avoid periodic crackdowns on their activities through their links, frequently familial, to the Ministry of Public Security, State Security Department, and/or Korean Workers' Party. Their reach even extends to rural areas.

This does not mean that people are bypassing the North Korean won and using foreign currency directly with traders at all times, since there are limitations that act to preclude this. Notably, there is an absence of low-denomination Chinese yuan and US dollar banknotes and coins, and the use of foreign currency is illegal and periodically enforced. As a result, in a lot of cases local currency is still used for market trading, whereas value is stored for periods longer than 24 hours in one foreign currency or another.

Conclusion

There is rising demand for foreign currency in the DPRK today, and as the Zairian case shows, this is a phenomenon directly linked to DPRK economic policy. There is a network of currency traders operating nationwide to meet this growing demand, exchanging currency in urban and, to a lesser extent, rural areas. This phenomenon makes a positive contribution to human security in the country. As such, it is worthy of careful consideration by all those who strive to build a better future for the people of the DPRK. **Y**

19 "Border Cities Love Chinese Yuan," *Daily NK,* April 17, 2013, http://www.dailynk.com/english/read.php?num=10496&cataId=nk03200.