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A Note on Economic Development in North Korea: Call for a Comprehensive Approach

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Abstract: North Korea is currently one of the most impoverished countries with a history of famine, but the country has a significant potential for economic development that could lift its population from poverty. Neighbored by some of the largest and most advanced economies in the world (South Korea, Japan, and China) and endowed with abundant mineral resources, industrial experience, and a history of successful economic development in the past, North Korea can embark on the path to rapid economic development, as its southern counterpart (South Korea) did so successfully since the 1960s. Yet, the successful economic development of North Korea requires a comprehensive approach, including obtaining a fund for development; normalizing relations with the West and the neighboring countries; improving its human rights conditions; prioritizing key industrial development; and reforming its political-economic system. This note discusses the comprehensive approach necessary for the successful economic development of North Korea.

Keywords: North Korea, economic development, human rights, industrial development

1 Introduction

North Korea, a mid-sized country located between South Korea and China, is presently one of the most impoverished countries in the world, with a per capita GNI of mere US\$1,295.¹ The country also suffered from a devastating famine causing the death of hundreds of thousands in the 1990s. Due to its repeated nuclear tests and ballistic missile test launches, North Korea is currently under heavy economic sanctions imposed by the United Nations and concurrently by a number of countries, including United States, Japan, the European Union, and

¹ Bank of Korea, *North Korea GDP Related Statistics*, available at: <<http://www.bok.or.kr/portal/main/contents.do?menuNo=200091>>, accessed July 22, 2018 (in Korean).

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South Korea. These sanctions put further pressure on its economy; North Korea reportedly recorded a minus 3.5% growth in 2017,² the lowest in twenty years since the 1990s.

Despite its bleak economic outlook, North Korea has a substantial economic potential; the country had the largest industrial complex in Northeast Asia built by Japan in the 1930s and gained experience in manufacturing industries.³ North Korea has a history of successful economic development and industrialization until the 1960s, as accounted by a Cambridge economist Joan Robinson,⁴ and its economy was known to be superior to its southern counterpart until the early 1970s.⁵ The country is also endowed with large deposits of mineral resources, including magnesite, zinc, tungsten, coal, iron, uranium, limestone, and rare earth minerals, valued at US\$6–10 trillion. North Korea also has an inexpensive, hard-working, and educated labor force.⁶

The impediments to the economic development of North Korea are economic governance and political factors, including its internal political-economic system and its relationship with the West and the neighboring countries. The socialist economic system that prohibits the private ownership of productive means, which does not allow producers to retain profits from production, has lowered individual incentives for production and has been ineffective for economic development. The totalitarian dictatorship has forced its population to be compliant with the government instructions, and there is no mechanism for internal checks and balances against the misguided economic policies once the central authority adopts them.

The continuing hostility with the West and lack of international support after the fall of the Soviet bloc drained its limited economic resources for costly military buildup, including developing nuclear weapons and ballistic

² *Ibid.*

³ For a discussion of the economic development of North Korea, see also Yong-Shik Lee, Young-Ok Kim, and Hye Seong Mun, “Economic Development of North Korea”, in Yong-Shik Lee *et al.* (eds.), *Law and Development Perspectives on International Trade Law* (New York: Cambridge University Press, 2011), pp. 356–375.

⁴ Joan Robinson, *Korean Miracle*, 16 *Monthly Review*, no. 9 (1965), 541–549.

⁵ Lee *et al.* (2011), *supra* note 3. However, there is also skepticism about the validity of economic statistics reported by North Korea during this period. Byung-Yeon Kim, Suk Jin Kim, and Keun Lee, *Assessing the economic performance of North Korea, 1954–1989: Estimates and growth accounting analysis*, 35 *Journal of Comparative Economics* (2007), 564–582, at 565.

⁶ Their productivity has been proven by, for instance, the successful operation of the Kaeseong Industrial Complex, which was a joint venture between South and North Korea from 2005 until its closure in 2016.

missiles.⁷ The continuing and increasing economic sanctions put heavy pressure on its trade and investment. In fact, the recent improvement of the North Korean economy, spurred by the expansion of private marketplaces and government policies granting a degree of autonomy and profit incentives to state corporations and collective farms, was halted in 2017 when the international sanctions were reinforced.

The current situation in North Korea requires a comprehensive approach for economic development. This note discusses this approach, including obtaining a fund for development; normalizing relations with the West and the neighboring countries; improving its human rights conditions; prioritizing key industrial development; and reforming its political-economic system.

2 Obtaining a Development Fund

Currently, North Korea lacks the financial resources to undertake projects essential for economic development. For example, its aging social infrastructure, such as roads, railways, bridges, harbors, power plants, and power grids, most of which were built several decades ago, needs repair and improvement.⁸ Many of its manufacturing plants are outdated and require substantial investments for improvement. Nevertheless, the North Korean government lacks financial resources to make these investments.⁹

The inadequate state of North Korea's infrastructure has impeded economic development; lack of electricity, caused by old and inefficient power plants and power grids, has created difficulties in the extraction of abundant mineral resources and the operation of factories. Its outdated inland transportation networks constrain the shipping of consumer and intermediate goods

⁷ An anonymous reviewer has noted that the extreme personal extravagance of the North Korean leaders, such as the purchase of large quantities of highest end Mercedes vehicles, as another reason for the economic drain. According to a report, the imported luxury items were distributed to the elites loyal to the leader as "gifts." Lee Jong-Heon, "Analysis: Kim's gift politics in challenge", UPI, 17 November 2006, available at: <<https://www.upi.com/Analysis-Kims-gift-politics-in-challenge/34551163774034/>>, accessed August 6, 2018.

⁸ The City Group estimated that the cost of the repair and improvement may amount to 71 trillion one, which is equivalent to approximately US\$64 billion. *Yonhapnews*, 28 June 2018, available at: <<http://www.yonhapnews.co.kr/bulletin/2018/06/28/0200000000AKR20180628052900009.HTML>>, accessed July 27, 2018 (in Korean).

⁹ North Korea's annual budget is estimated as US\$7.3 billion in 2017. Ministry of Unification, *North Korea Information Portal*, available at: <<http://nkinfo.unikorea.go.kr/nkp/overview/nkOverview.do?sumryMenuId=EC208>>, accessed July 27, 2018 (in Korean).

and raw materials. The repair and improvement of North Korea's social infrastructure and manufacturing plants, which are imperative for the economic development of North Korea, will require a substantial amount of financial resources. North Korea also needs financial resources to import raw materials, machinery, and other types of goods, and also to acquire and develop new technologies.

How may North Korea obtain the financial resources to meet the needs for economic development? Possible sources include loans, aids and grants, and other forms of support from the international financial institutions, such as the World Bank, commercial banks operating internationally, and other governments willing to support North Korea's economic development, such as South Korea. However, many of these sources will not be available until the economic sanctions, which currently prohibit these entities from engaging in financial transactions with North Korea,¹⁰ are lifted. The political-economic interests of South Korea and the United States create another unique opportunity for North Korea to obtain a substantial amount of financial resources.

With the cooperation from South Korea and the United States, the North Korean government will be able to issue a substantial amount of bonds in an open market, again, after the current economic sanctions are lifted. North Korea does not have a sufficient credit to issue bonds that will be in demand in the international financial market. However, South Korea has a large and prosperous economy, and possesses such credit, as proven by the successful issuances of bonds in the recent years¹¹; North Korea will be able to issue bonds if the South Korean government concurrently offers payment guarantee in the case of default.

The South Korean government will have an interest to offer such guarantee if the North Korean government agrees to transfer the mining rights to some of its abundant mineral resources to South Korea in return, and to additional mineral resources in the case of default.¹² Since the South Korean government has its own interest in improving North Korea's social infrastructure and accessing abundant mineral resources in North Korea, with the view of sharing

¹⁰ U.N. Security Council Resolution 2094 (2013), paras. 11, 14 and Council Resolution 2087 (2013), para. 6.

¹¹ In 2014 and 2017, South Korea was able to issue foreign exchange equilibrium bonds in the amount of US\$2 billion and US\$1 billion with 30-year maturity and 10-year maturity, respectively.

¹² An anonymous reviewer has commented on a risk that North Korea may ignore the arrangement and revoke the mining rights granted to South Korea once it obtains the fund, but this will not be in the interest of North Korea, as it undermines its own credibility and is likely to deter further investment from the West.

benefits from economic development in North Korea,¹³ this type of transaction could be supported by the Korean constituencies if the terms are appropriate. The amount of the bonds raised could be substantial, up to \$30 billion, which would be equivalent to 5% of the lower end of the deposit value of the mineral resources in North Korea. This could cover a substantial portion of the cost needed to repair and improve North Korea's social infrastructure and manufacturing facilities.

3 Normalizing Relationship with the West and the Neighboring Countries

The issuance of bonds discussed in the preceding section, as well as the other types of financial support for economic development of North Korea, will not be possible unless North Korea improves its relationships with the international community and the neighboring countries, such as South Korea, Japan, the United States (through military presence in South Korea), China, and Russia. Although China and Russia are North Korea's traditional supporters, they have objected to North Korea's nuclear development and ballistic missile test launches and have joined the recent economic sanctions imposed by the United Nations.¹⁴ North Korea has engaged in dialogues with South Korea, the United States, and Japan for the past several decades, including the recent summit meetings with South Korea and the United States, but its relationship with these countries has remained confrontational and hostile, blocking the possibility of extensive economic engagement with these countries.

It is a major loss of an important economic opportunity for North Korea, given the economic capacities of these countries – the United States is the largest economy in the world, Japan the third, and South Korea the 11th; these countries are also among the largest traders in the world. South Korea, which suffered from economic deprivations until the early 1960s, benefitted tremendously by engaging with the United States and Japan in trade and

¹³ The South Korean President Moon Jae-in reportedly offered the head of North Korea Kim Jong Un a plan for economic integration between South and North Korea in the April 2018 summit meeting. See "Seoul offers Kim Jong-un grand bargain to link North and South Korean economies with China", *South China Morning Post*, 7 May 2018, available at: <<https://www.scmp.com/news/china/diplomacy-defence/article/2145052/seoul-offers-kim-jong-un-grand-bargain-link-north-and>>, accessed July 30, 2018.

¹⁴ See *supra* note 10.

investment and was able to lift its economy to the status of one of the most advanced in the world.¹⁵ In addition, the current economic sanctions, which render trade and investment with North Korea virtually impossible, except narrow exceptions,¹⁶ will not be lifted unless North Korea's relationships with the international community improve, including these countries. With the current sanctions in place, economic development of North Korea will be very difficult, as shown by the sharp economic decline in 2017. The North Korean economy had shown major improvement, aided by the spread of private marketplaces and the government policies endorsing them and granting market incentives to state corporations and farms,¹⁷ but the heavy sanctions took a toll and reversed the trend.¹⁸

North Korea is facing the need to make a strategic decision on its nuclear arsenal and ballistic missiles, and it began to take steps by meeting the Presidents of South Korea and the United States and agreeing that it will work toward a denuclearized Korean peninsula.¹⁹ North Korea expressed a concern that the regimes of the countries that abandoned nuclear arms projects, such as Iraq and Libya, subsequently collapsed, and North Korea might follow suit if it gives up their own nuclear arsenal

15 In 1962, South Korea's GNI per capita was US\$120, among the lowest in the world with the majority of its population stricken with poverty. By 1996, South Korea had become an advanced developed country with an affluent economy and world-class industries; its per capita GNI reached US\$13,040 classified by the World Bank as a high-income country at that time, and Korea became a major industrial power and leading trader, joining the ranks of the other advanced countries in Europe and North America at the OECD. Yong-Shik Lee, *General Theory of Law and Development*, 50 Cornell International Law Journal, no. 3 (2017), 415–472, at 461.

16 *Supra* note 10.

17 In 2012, the North Korean government adopted a series of measures (“June 28 measures”) to adopt market incentives and allow a degree of managerial discretion to state corporations, such as discretion to retain and dispose of surplus products exceeding state quotas in the marketplaces. Park Hyeong Jung, “Will North Korea’s “6.28 Directives” Be a Prelude toward “Reform and Opening”?”, KINU Center for North Korean Studies, Online Series CO 12–31, available at: <<http://repo.kinu.or.kr/bitstream/2015.oak/2140/1/0001453774.pdf>>, accessed July 16, 2018.

18 North Korea's growth rate was reportedly down to –3.5% in 2017 from 3.9% in 2016, due to the strengthened economic sanction that substantially cut exports and the drought that reduced electrical power generation from hydroelectric power plants. Voice of America, “North Korea's Economic Growth in the Last Year Worst in the 20 Years”, 20 July 2018 (in Korean), available at: <<https://www.voakorea.com/a/4490865.html>>, accessed July 20, 2018. The Bank of Korea, Press Release, no. 2018-7-17 (21 July 2018) (in Korean).

19 *The Panmunjeom Declaration*, 27 April 2018, para. 3:4 and *the U.S.-North Korea Agreement*, 12 June 2018, para. 3.

without security guarantees from the West.²⁰ However, this concern seems to have been misplaced; Iraq was invaded by the United States and its allies, and its regime collapsed after the invasion, but a major military invasion into North Korea by the West, in absence of a direct threat to its own security, would not be feasible, given North Korea's geographic proximity to the heartland of China, South Korea, and Japan, and considering the strong objections by China and Russia. In the case of Libya, nuclear weapons, even if the Gathafi regime had possessed them, would not have prevented the popular uprising, just as the Soviet Union, armed with massive nuclear weapons, could not stop their own. The lift of current economic sanctions and the improvement of North Korea's relationship with the West and the neighboring countries, which will be imperative to the economic development of North Korea, will be difficult without the resolution of the nuclear issue.

4 Improving Human Rights Conditions

Another factor that impedes economic engagements with the West will be the issues associated with North Korea's human rights conditions. According to a U.N. investigation report,²¹ hundreds of thousands of political prisoners and their families are currently detained in political prison camps, and human rights violations, such as torture (including forced medical experiments), arbitrary detention, public executions, and forced disappearances, are prevalent in North Korea, over the confirmed or suspect incidents of expressing political disagreement, not involving any violent crime. In addition, the report cites restrictions of a wider range of civil rights, such as freedoms of thought, expression, and religion; and freedom of movement and residence

²⁰ "North Korea Claims that Iraq and Libya Collapsed due to the Abandonment of Nuclear Weapons", Yonhapnews, 8 January 2016, available at: <<http://www.yonhapnews.co.kr/bulletin/2016/01/08/0200000000AKR20160108169200014.HTML>>, accessed July 29, 2018 (in Korean). In addition to Iraq and Libya, Ukraine also gave up its nuclear arsenal on the written security guarantees of the United State and the United Kingdom, but the latter failed to protect the security of Ukraine when it was invaded by Russia in 2014. See Michael Kofman, Katya Migacheva, Brian Nichiporuk, Andrew Radin, Olesya Tkacheva, and Jenny Oberholtzer, *Lessons from Russia's Operations in Crimea and Eastern Ukraine* (Santa Monica, CA: RAND Corporation, 2017), available at: <https://www.rand.org/pubs/research_reports/RR1498.html>, accessed August 6, 2018.

²¹ United Nations, Human Rights Commission, *Report of the detailed findings of the commission of inquiry on human rights in the Democratic People's Republic of Korea*, A/HRC/25/CRP.1 (7 February 2014).

with severe penalties imposed by the state for violating state instructions in these matters.²² North Koreans are also subject to discriminatory treatment by the state in accordance with their class imposed by the state (called “Sungbun” in North Korea).²³

The issues with the human rights conditions have direct economic impact; North Korea denies the occurrence of human rights violations and maintains that such matters are a domestic affair not to be interfered with by foreign powers,²⁴ but the content of the report has been corroborated extensively by multiple sources, including a number of testimonies by former residents. Given the gravity of the issue, some of the current economic sanctions have built-in provisions that do not allow the lifting of the sanctions without the improvement of the human rights conditions.²⁵ Beyond the sanctions, the negative reports of the human rights conditions will create practical difficulties for potential investors and traders, particularly those in the West, from engaging with North Korea, for their own corporate social responsibility requirements against unethical practices, including trade and investment with the facilitator of serious human rights violations.

The improvement of the human rights conditions is also necessary to retain North Korea’s human capital needed for economic development. The serious human rights conditions, as well as economic deprivations, have prompted hundreds of thousands of able North Koreans to escape from the country for destinations in China, South Korea, and other places, despite the strict border control and harsh punishment for those attempting to leave the country. Many of these North Korean migrants became successful in other countries, becoming best-selling authors, doctors, engineers, and teachers, and retaining this human capital would be in the interest of North Korea in promoting economic development. To retain human capital, it will not be sufficient to increase control over the population, reinforce the border watch, and strengthen punishment for the escapees. The improvement of human rights conditions will remove a significant cause of migration and will be helpful to retain human capital within the country.

²² *Ibid.*

²³ *Ibid.*

²⁴ Park Soo Hyun, “North Korea Claims that the U.N. Human Rights Report has been fabricated by the information supported by hostile powers”, *Chosun Ilbo*, 20 June 2018, available at: <http://news.chosun.com/site/data/html_dir/2018/06/20/2018062002006.html>, accessed July 29, 2018 (in Korean).

²⁵ For example, the North Korea Sanctions Policy Enhancement Act of the United States includes specific references to human rights, including provisions for mandatory designation.

5 Prioritizing Key Industrial Development

For the successful economic development of North Korea, it is essential to prioritize key industrial development, such as manufacturing industries. North Korea has been focusing on building tourist sites, such as rebuilding Pyongyang, constructing a ski resort in Masikryong, and converting the City of Wonsan, the birthplace of the new leader, Kim Jeong Un, into a major tourist attraction, mobilizing hundreds of thousands of soldiers and para-military workers (called “Dolgyukdae”) as laborers to build these projects. Although the tourist sites are visible and attractive, it is not likely to generate the level of employment and industrial development necessary for the successful economic development of North Korea.

By contrast, its southern neighbor, South Korea, focused on building manufacturing industries, rather than tourist sites, and was able to transform its economy, which was one of the poorest in the world in the early 1960s, to one of the most advanced and affluent by the 1990s, generating a large number of jobs and higher income for the majority of its population.²⁶ South Korea adopted the state-led development strategies, providing government support, such as tax breaks and loan guarantees, as well as trade protections, to the industries that were conducive to economic development and were feasible to develop given the level of capital and technology available at the time; *i. e.*, light industries (*e. g.*, textiles) in the 1960s; heavy and chemical industries in the 1970s; and electronics in the 1980s. To overcome the limits of the small domestic markets, South Korea focused on exports, and the industries initially supported by the government became self-sufficient and prosperous in the domestic and overseas markets.²⁷

²⁶ See *supra* note 15. See also Yong-Shik Lee, *Trade and Development: Lessons from Korea*, 25 *Korean Journal of International Trade and Business Law*, no. 2 (2016), 51–76 and Yong-Shik Lee, *Law and Development: Lessons from South Korea*, 11 *Law and Development Review*, no. 2 (2018), 433–465.

²⁷ For a further discussion of export-led development models, see A. O. Krueger, “Trade Policies in Developing Countries”, in R. W. Jones and P. B. Kenen (eds.), *Handbook of International Economics*, vol.1 (North-Holland, New York, 1984), pp. 519–569; R. Findlay, “Growth and Development in Trade Models”, in R. W. Jones and P. B. Kenen (eds.), *Handbook of International Economics*, vol.1 (North-Holland, New York, 1984), pp. 185–236; T. N. Srinivasan, *Trade, Development, and Growth*, Princeton Essays in International Economics, no. 225 (December 2001); G. K. Helleiner (ed.), *Trade Policy, Industrialization, and Development* (Oxford University Press, Oxford, 1992); and World Bank, *The East Asian Miracle* (Oxford University Press, New York, 1993).

The example of the South Korean development provides a reference for North Korea.²⁸ North Korea has advantageous economic conditions that were not available to South Korea when it initiated economic development in the 1960s; South Korea had to rely almost entirely on the imports of crucial mineral resources for its industrial development and had to use its hard-earned cash from exports to acquire these resources, experiencing trade deficits until the 1980s. In contrast to South Korea, North Korea has abundant mineral resources that can be used for its own industrial development. Unlike the least-developed countries elsewhere, North Korea also has substantial industrial experience and an inexpensive, hard-working, and educated labor force ready to be deployed in the manufacturing sector.

Additionally, North Korea has a unique geographic advantage for economic development, being a neighbor to the second largest export market in the world, China, to the north and the potential source of advanced technologies and capital, South Korea, to the south. South Korea is willing to provide economic assistance,²⁹ subject to the resolution of the current nuclear crisis and the improvement of North Korea's relationship with the West, which is necessary for the removal of the sanctions. Additional economic powerhouses, such as the United States and Japan, have also expressed their willingness to engage North Korea economically, again, subject to the resolution of the current security issues.³⁰ The presence and potential availability of these economies are conditions that are favorable to promote the economic development of North Korea, and it will be advisable to devise a development plan that will prioritize industrial development utilizing these favorable conditions.³¹

6 Reforming Political-Economic System

In the major joint venture between South and North Korea, the Kaeseong Industrial Complex ("KIC"), North Korea received only a fraction of the revenue generated by the KIC, because North Korea provided only laborers while South Korea sent private corporations to hire them and was able to retain the major

²⁸ See also Lee *et al.* (2011), *supra* note 3.

²⁹ *Supra* note 13.

³⁰ Josh Delk, "Pompeo: US will help North Korea's Economy if it Forfeits Nukes", The Hill, 11 May 2018, available at: <<http://thehill.com/policy/international/387330-pompeo-offers-economic-aid-in-exchange-for-north-korean-nukes>>.

³¹ See also Lee *et al.* (2011), *supra* note 3.

portion of the revenue after paying the modest wages to the North Korean workers. The socialist economic system of North Korea does not approve the private ownership of productive means, including corporations, and when the KIC was shut down in 2016 for political reasons, the industrial experience of the KIC could not be transferred elsewhere in North Korea, and its contribution to the economic development of North Korea was limited.

To promote economic development of North Korea, it is necessary to adjust its political-economic system, including the socialist approach to the ownership of corporations. By contrast, other more successful socialist countries, such as China and Vietnam, approve the private ownership of corporations³² to utilize the profit-maximization-motive and have successfully developed their economies. Adjustments should also be made to the other restrictions imposed on its population, such as the restrictions on the movement of people and residence; this is to secure the mobility that is necessary to enhance economic transactions. Access to information and freedom to utilize that knowledge is also important to develop new businesses and improve the efficiency of the existing ones; yet, the restrictive political and social environment in North Korea in which the state monitors individuals, surveilling their conduct, including speech, will not be conducive to nurturing the innovative and efficient culture necessary for economic development. As discussed,³³ the totalitarian dictatorship compels its population to be compliant with the government instructions, and there is no mechanism for internal checks and balances against the misguided economic policies once adopted by the central authority.

The North Korean political leaders, who have enjoyed the unchallenged absolute power for over seven decades, may deem the suggested reforms, including the improvement of human rights conditions and the adjustment of political-economic system, as weakening their control over the population, creating a potential threat to the security of their regime. The dilemma is that without these reforms, it will be difficult for North Korea to achieve sustained economic development that will lift its population from poverty to prosperity. The development model known to be a preference for the North Korean leaders, such as Singapore, may have maintained an authoritarian rule, but the degree of civil liberty, the rule of law, and the country's openness to the outside world are not comparable to North Korea. The resolution of the nuclear crisis is more of a short-term issue, but these reforms are a fundamental one that will determine

³² *Ibid.*, at 372.

³³ See discussion *supra* Section 1.

the success of the economic development of North Korea. Political powers tend not to give up its own powers, but it remains to be seen whether the current North Korean leaders will be willing to take the steps towards the necessary reforms for economic development, which they have claimed to be a top priority, and risk weakening their power and control over the nation.³⁴

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³⁴ Song Sang-ho, "North Korean Leader Shifts Policy Focus to Economy", *Yonhapnews*, 21 April 2018, available at: <<http://english.yonhapnews.co.kr/news/2018/04/21/0200000000AEN20180421002500315.html>>, accessed July 29, 2018.

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