

**NORTH KOREA: STATUS REPORT ON NUCLEAR PROGRAM,
HUMANITARIAN ISSUES, AND ECONOMIC REFORMS**

A STAFF TRIP REPORT
TO THE
COMMITTEE ON FOREIGN RELATIONS
UNITED STATES SENATE

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Letter of Transmittal

February 23, 2004

The Honorable Richard Lugar
Chairman, Committee on Foreign Relations.

The Honorable Joseph R. Biden,
Ranking Member, Committee on Foreign Relations.

Dear Senators Lugar and Biden:

In early January, we traveled to China, North Korea, South Korea, and Japan, to assess the prospects for a peaceful negotiated solution to the North Korean nuclear issue and to follow-up on three earlier visits to North Korea focused on gaining more transparency on food aid issues and encouraging greater North Korean adherence to international norms in the area of human rights. We met with foreign government officials as well as with professors and think tank specialists concerned with developments on the Korean Peninsula.

While in North Korea, we visited the Yongbyon nuclear facility along with Dr. John Lewis of Stanford University, Jack Pritchard of the Brookings Institution, and Sig Hecker, former Director of Los Alamos Nuclear Laboratories. We also requested of North Korean officials and were granted meetings to afford us an opportunity to engage in detailed discussions on a number of humanitarian issues, including food aid, prison conditions, and the Japanese abduction cases. We also traveled to Seoul and Tokyo to meet with key officials. We wish to acknowledge the efforts of officials at the State Department in Washington and abroad who helped to facilitate our travels.

A report on our major activities and key findings, including some thoughts about the next steps on the Korean Peninsula, follows below.

Sincerely,

Keith Luse
Professional Staff Member, Majority Staff
East Asian and Pacific Affairs
Senate Foreign Relations Committee

Frank Jannuzi
Professional Staff Member, Minority Staff
East Asian and Pacific Affairs
Senate Foreign Relations Committee

NORTH KOREA: STATUS REPORT ON NUCLEAR PROGRAM, HUMANITARIAN ISSUES, AND ECONOMIC REFORMS

Executive Summary

Senate Foreign Relations Committee (SFRC) staff members Keith Luse and Frank Jannuzi traveled to China, North Korea, South Korea, and Japan January 3-15 to assess the prospects for a peaceful negotiated solution to the North Korean nuclear issue and to follow-up on earlier visits to North Korea designed to encourage greater North Korean transparency on food aid and greater adherence to international norms of behavior on a broad array of human rights issues.

While in North Korea, our delegation interacted with a group of three private citizens – Dr. John Lewis of Stanford University, Jack Pritchard of the Brookings Institution, and Sig Hecker, former Director of Los Alamos Nuclear Laboratories – and accompanied them to the Yongbyon nuclear facility. This marked the first time North Korea has allowed foreigners to enter its key nuclear facilities since it expelled IAEA monitors in December, 2002. We have relied on the observations of Dr. Hecker to convey key findings from Yongbyon. Dr. Hecker's testimony to the Senate Foreign Relations Committee is attached to this report.

Over the course of five days in the North, we held a variety of meetings with DPRK officials to discuss their nuclear program and to encourage greater North Korean respect for human rights. The delegation sought to clarify North Korea's December 9 offer to "freeze" its nuclear program, and urged North Korean officials to abandon their pursuit of nuclear weapons and seek a peaceful, negotiated solution to the crisis through multilateral dialogue.

While at Yongbyon, Dr. Hecker was able to confirm that the 5MWe nuclear reactor is running normally and that the 8,000 spent fuel rods which had been stored under International Atomic Energy Agency supervision under the terms of the 1994 Agreed Framework have been removed from their canisters and are no longer in the spent fuel storage facility. Our tour of the Radiochemical laboratory also convinced Dr. Hecker that North Korea has the *capability* to reprocess spent fuel and produce plutonium metal. North Korea did not make available any DPRK personnel who may have expertise in nuclear weapons design and manufacture, and Dr. Hecker reached no conclusions about the North's ability to build a nuclear device.

During a discussion with Foreign Ministry officials on the North's nuclear program following our time at Yongbyon, Vice Foreign Minister Kim Gye-gwan claimed that unlike Iran and Libya, North Korea actually *has* weapons of mass destruction. Kim said that North Korea had provided us with evidence of their "nuclear deterrent." These were the most explicit statements we received that North Korea has produced nuclear weapons.

As for U.S. allegations that North Korea has a clandestine program to produce highly enriched uranium (HEU), Kim Gye-gwan and other DPRK officials stated categorically that the DPRK has no program for enriching uranium.

On the human rights front, Luse and Jannuzi had the opportunity to engage in detailed discussions on a number of issues, including food aid, prison conditions, and the abduction of Japanese nationals by North Korean intelligence agents. We emphasized that the United States' concern for the human rights situation in North Korea reflects the deeply held convictions of the American people. SFRC staff encouraged DPRK officials to permit greater transparency for food aid deliveries under the auspices of the World Food Program and various non-governmental organizations, and we discussed ways in which North Korea might reduce its dependence on foreign food aid by adopting new methods of food production and moving toward market-based distribution mechanisms. The delegation pressed DPRK officials to allow outside access to its prison facilities to assess food needs and humanitarian issues there. We also met with Foreign Ministry officials to express our hope that North Korea would take steps to fully resolve the issue of the past abduction by the DPRK of more than a dozen Japanese nationals. We explained that the prompt resolution of this issue was a matter of international concern and of particular interest to members of the Congress. The delegation requested information on the abductees and their family members still in North Korea and passed this information on to the Japanese government.

Finally, the delegation had a chance to review the progress of North Korea's economic reforms launched in July of 2002. We found considerable evidence that North Korea is committed to moving toward a market economy, but it is too soon to draw conclusions about the ultimate success or failure of these initiatives. North Korea suffers from critical resource shortages and it may not yet fully grasp the institutional changes that will be necessary if its fledgling economic reforms are to yield a significant boost in DPRK production and an improvement in living standards for the North Korean people. Even if North Korea's economy begins to grow, it is not clear how this will affect the nation's social and political stability. Officials with whom we met recognized that the North's ability to expand trade and attract foreign investment and receive loans from international financial institutions depends in large measure on the peaceful resolution of the nuclear issue.

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North Korea's Nuclear Program

Prior to our visit to Yongbyon, Vice Foreign Minister Kim Gye-gwan told us that North Korea had decided to permit our visit to break through the “stalemate” at the six party talks and to provide “more transparency on our nuclear program that has been shrouded in mystery.” Kim also said North Korea hoped to differentiate its nuclear program from those pursued by Libya and Iran. “They claim they do not have weapons of mass destruction. We claim that we do have weapons of mass destruction, and we leave the conclusions to your side.”

Kim said that North Korea had chosen to reprocess the 8,000 spent fuel rods from its nuclear reactor to “strengthen our deterrence” in response to the “intensifying hostile policy” of the U.S. government. He specifically cited the President’s reference to North Korea as a member of the “Axis of Evil,” as well as the inclusion of North Korea in a list of countries subject to “pre-emptive strike” by the United States. Kim told the delegation that he believes only the North’s nuclear deterrent has prevented the United States from launching a pre-emptive attack. “Once we lay down our gun, the United States would attack immediately.”

Nonetheless, Kim repeatedly stated that North Korea remains interested in the “final goal” of a nuclear free Korean Peninsula, and said, “If we are to reach the final goal, we need to become serious about specific action steps, not just talk. A freeze of current activities might be a first step. At Yongbyon, you will see the importance of a freeze. We are prepared to give up our nuclear activities, have no transfer to other nations, and no testing of any kind. We truly believe this is the right place to start.” Kim later clarified that the North’s freeze proposal “only makes sense as a starting point to reach the objective of a non-nuclear peninsula. We don’t want to stop at a freeze.” He also emphasized that “how to freeze” and “what comes next” are issues the North hopes can be discussed in detail at the next round of six party talks, and that North Korea is “...fully open to these kind of talks.”

Our delegation raised the question of the North’s alleged program to develop highly enriched uranium (HEU). Kim Gye-gwan stated categorically that the DPRK “has nothing to do with any HEU program.” Kim said, “We have no program, no facilities you are talking about, or scientists trained for this purpose [enriching uranium].”

Kim Gye-gwan continued, “Our policy on nukes is based on natural uranium, not highly enriched uranium...We don’t have any plans for HEU or facilities for that purpose.” Moreover, Kim flatly denied that North Korea had ever admitted to having an HEU program during the October, 2002 meeting with Assistant Secretary of State James Kelly in Pyongyang.

[Yongbyon Visit](#)

On Thursday, January 8, we spent roughly six hours at the Yongbyon nuclear facility. Yongbyon is about two hours by car from Pyongyang, with much of the last hour spent on unpaved roads. The Yongbyon nuclear complex is a city unto itself. DPRK officials said that about 1,000 scientists and technicians work and reside at the facility, and several thousand others provide support services, grow food, etc. During our visit, we were at all times escorted by senior officials at Yongbyon as well as by Ambassador Li Gun, our Foreign Ministry host.

Of the five Americans who visited Yongbyon, only Dr. Hecker possesses detailed understanding of the workings of a nuclear power plant and the science connected with the extraction of plutonium from spent reactor fuel and the production of plutonium metal. Dr. Hecker's expertise allowed him to ask probing questions and to engage in expert level discussions with his counterparts. Accordingly, we have not tried to make any independent assessments of the North's nuclear capabilities. We are relying on Dr. Hecker's findings, and will make only a few general observations about the tenor of our visit.

North Korean officials at Yongbyon exhibited an easy confidence during our tour, answering questions promptly and with thoroughness. They seemed eager to showcase their facilities and what they had accomplished. Yongbyon facility director Ri Hong-sop told us that North Korea's nuclear program was developed indigenously. In response to a question, Ri denied that North Korea had provided any nuclear technology to Burma or any other country.

The DPRK scientists confined their remarks and exchanges to the science of running a nuclear reactor and fabricating plutonium, generally avoiding political remarks or debate. Their tone and demeanor were professional. The North's officials appeared open to a repeat visit by Dr. Hecker to help confirm what we had seen through additional observations and scientific measurements.

Yongbyon Key Findings

Dr. Hecker's key findings based on our visit to Yongbyon are these:

- The 5 MWe reactor has been restarted. It appears to be operating smoothly providing heat and electricity, while also accumulating approximately 6 kg of plutonium per year in its spent fuel rods.
- The 50 MWe reactor construction site appears to have seen no activity since the IAEA inspectors were instructed to leave in 2002. The reactor and the construction site look in a bad state of repair. It would require a major construction program to finish the reactor. North Korea reports the future of the 50 MWe reactor is still "under evaluation."
- The spent fuel pond is empty; the approximately 8000 fuel rods have been moved.
- The DPRK claimed to have reprocessed all 8000 fuel rods to extract plutonium metal during one continuous campaign between mid-January 2003 and end of June 2003. We could not definitively substantiate that claim. *However, the Radiochemical Laboratory*

staff demonstrated that they had the requisite facility, equipment and technical expertise, and they appear to have the capacity to extract plutonium from the spent fuel rods and fabricate plutonium metal. If all 8000 fuel rods were reprocessed, the IAEA estimates they would provide 25 to 30 kg of plutonium.

- It is possible that they moved the 8,000 fuel rods to a different storage location. However, such storage would represent a serious health and safety hazard.
- We were shown what was claimed to be a sample of plutonium metal product produced last year. Dr. Hecker was not able to definitively confirm that the sample was actually plutonium metal, but all observations he was able to make were consistent with the sample being plutonium metal. However, Dr. Hecker was not able to prove that the samples were from the most recent reprocessing campaign. Such a determination requires more sophisticated measurements.
- In the foreseeable future, the DPRK can produce 6 kg of plutonium per year in its 5 MWe reactor. It easily has the capacity to reprocess the spent fuel at any time to extract the plutonium. It also has the capacity to reload the reactor with fresh fuel for a second and subsequent reloading. Unless North Korea has a clandestine nuclear reactor, it appears the DPRK is not in a position to increase the rate of plutonium production beyond 6 kg per year without a major construction project at the 50 MWe or 200 MWe reactor sites.
- Officials of the DPRK Ministry of Foreign Affairs claimed that the DPRK had weapons of mass destruction. They believe that they provided us with evidence of their “nuclear deterrent.” At Yongbyon, they demonstrated that they most likely had the capability to make plutonium metal. However, Dr. Hecker saw nothing and spoke to no one who could convince him that they could build a nuclear device with that metal, and that they could weaponize such a device into a delivery vehicle. We were not able to arrange meetings with DPRK staff who may have such expertise or visit related facilities.

Humanitarian Issues

Upon arriving in Pyongyang, staffdel asked our host, Ambassador Li Gun to arrange meetings on the topics of the Japanese abductee issue, prison camps in North Korea and their conditions, and food aid to the DPRK. These on-the-spot requests were all accommodated.

Japanese Abductees

In 2002, Kim Jong-il acknowledged to Japanese Prime Minister Koizumi that North Korean agents had abducted 13 Japanese nationals during the 1970's and 1980's. Japanese officials contend the number could go much higher. (South Korean officials estimate that several hundred South Koreans have been abducted by the North over the years, most never to return). The Japanese were abducted reportedly to teach Japanese language and culture to North Korean spies. At least five of the Japanese abductees remain alive and were returned to Japan last year following the Kim Jong-il - Koizumi summit. North Korean and Japanese officials continue to negotiate as to the fate of children and other relatives of these five, as well as eight additional Japanese abductees reported dead by North Korean authorities. North Korea has not provided evidence convincing to the Japanese that the remaining eight are deceased.

The North Korean official with whom we met on the abductee issue was Song Il-ho, Deputy Director of the Foreign Affairs Ministry for Japan. We emphasized that the United States' concern for the human rights situation in North Korea – including the fate of those abducted by North Korea and their families – reflects the deeply held convictions of the American people. We expressed our hope that North Korea would promptly take steps to fully resolve the issue, and explained the welfare of the abductees and their families was a matter of international concern and of particular interest to members of the Congress. We emphasized that we were not in North Korea to negotiate, but only to exchange views.

Song gave his government's perspective on the abductee issue, beginning with an overview of Japan-Korea relations from the colonial period to the present. After this background, Song acknowledged that North Korean secret agents did wrongly abduct Japanese nationals. “[They] did bring Japanese nationals to the DPRK. Thirteen were brought to the DPRK, some of whom have died of accidents or illness. Those responsible for bringing them here were charged under state law and punished.”

After conveying his government's views, Song was forthcoming in answering questions we asked about the abductees and their relatives. He expressed his willingness to answer additional questions in the future. Song reported that Japan has been provided with videotapes and other information pertaining to the children and other relatives of the abductees remaining in North Korea. Song said that some of the abductees' children only recently became aware of the truth regarding their parents' origin, adding that the children have close relationships in his country, (including fiancees for some), have never been outside North Korea, and should be able to make individual decisions on whether they remain in North Korea or go to Japan. (Japanese officials counter that all abductees and their immediate relatives should be able to travel to Japan to live for a set amount of time before deciding on their own whether they would remain in Japan or return to North Korea.)

U.S. Food Assistance to DPRK

As we did last August, we met again this year with Jong Yun-hyong, Director of the Flood Damage Reconstruction Committee, who is working with American and European NGO's and universities to expand efforts toward sustainable agriculture. During our meeting, Jong for the first time made reference to the topic of "rural development," indicating that non-government organizations (NGO's) may be designated to take charge of small to medium-sized rural development projects in the areas of energy and agricultural production.

Poor farming practices are evident in DPRK. Soybeans, corn and orchards planted vertically on mountainsides contribute to erosion. Poorly-built levees break during heavy rains causing fields to flood. There are often inadequate amounts of fertilizer and the soil is over-worked. Double-cropping is practiced throughout the country. North Korea is interested in adopting better agricultural practices.

Although anxious to achieve food production self-sufficiency, Jong acknowledged emergency assistance will be needed for quite some time given the North's shortage of arable land. He expressed gratitude for the recent announcement from the U.S. of additional food aid. When the staff delegation once again questioned Jong on DPRK not allowing the World Food Program (WFP) to fully monitor food distribution and the lack of access to children, the elderly and pregnant women in 43 counties, he responded by advocating a shift away from food assistance and toward agriculture development projects.

Jong outlined the North's food production and distribution for 2003. He reported that the North produced 4.5 million metric tons of grain (primarily rice, corn, wheat and barley). The DPRK calculates that after making allowances for food grain consumption, seed grain, livestock consumption, restaurant services, and spoilage, the North's production will fall roughly one million tons short of its needs for 2004. The Public Distribution System (PDS) largely broke down during the famine years of the mid-1990's, and has never fully recovered. Most North Koreans reportedly receive a meager allotment (300 grams/day) from the PDS, and must supplement their allotment with purchases of food from markets. Jong expressed his hope that the World Food Program and other donors would help close the gap between the North's production (including imports) and its actual food needs.

Kim Jong-il maintains a "military-first" policy in terms of food produced in North Korea, and Jong acknowledged that the military gets preferential access to the harvest. Once its needs are met, remaining food production enters the PDS. Given the minimal monitoring of bilateral South Korean and Chinese food aid (largely rice), we believe it is possible that North Korea may divert a portion of the rice from those two countries to meet any unfulfilled needs in the military for 2004, as it likely has in the past.

The United States provides food assistance to North Korea through the World Food Program (WFP), which targets its aid to the elderly, children up to the age of 10 and pregnant and nursing women. In February, 2003, the U.S. government announced its intention to provide 100,000 tons of food assistance in calendar year 2003, with 40,000 tons to be shipped immediately and 60,000 tons to be shipped depending on circumstances inside North Korea and on competing global demands for assistance. On December 24, 2003, the Administration announced it would ship the last 60,000 metric tons. This assistance package will reportedly include 38,000 metric tons of corn, 4,000 metric tons of non-fat dry milk, 6000 metric tons of corn-soya blend, 6000 metric tons of vegetable oil, with the remaining products including peas and beans. U.S. AID officials believe these food items are more apt to reach the hungry target groups than U.S. rice.

Most of the recipients of WFP aid live in urban areas outside of Pyongyang. WFP staff now conduct about 500 monitoring visits in North Korea per month, although most visits must be scheduled one week in advance and monitors are usually accompanied by North Korean officials. WFP has five field offices outside of Pyongyang. North Korea still does not permit WFP to feed the hungry in 43 out of 206 counties, mostly due to national security considerations. These off-limits counties are estimated to contain 15% of North Korea's population. WFP has no good information on the food needs of these counties, most of which are in mountainous regions of north-central DPRK or clustered along the border with South Korea (adjacent to the DMZ).

Over time, the WFP's ability to monitor its food aid deliveries has improved. WFP personnel are now able to obtain Korean-language training inside North Korea, and WFP has dramatically increased the number of monthly inspection visits over the past three years. WFP has also chosen to curtail food aid in Pyongyang. This is appropriate, as Pyongyang residents are typically better off than residents of other parts of North Korea. WFP has issued an appeal for 485,000 tons of commodities for 2004, a decrease from 513,000 tons sought for 2003. Only 300,000 tons of the amount requested for 2003 was actually received and distributed.

An extensive nutrition survey conducted last year showed significant reductions in malnutrition among young children since 1998, a decrease due in large part to outside food assistance. However, even with gains in nutrition standards, more than 40% of North Korea's children under the age of seven are markedly too short for their age – stunted – a condition largely irreversible with an impact on mental growth yet to be measured.

The Gulags

During our trip to North Korea last August, we raised the issue of the prison system and the poor conditions and high levels of malnutrition reported there with Vice Foreign Minister Kim Gye-gwan. An estimated 150,000-200,000 North Koreans reportedly are held under harsh conditions in hundreds of political detention camps. Last year, Kim Gye-gwan said that North Korean officials would allow non-government organizations (NGO) access to prison camps on a "case by case" basis.

During our recent trip to Pyongyang, we once again raised this issue with North Korean officials including Ambassador Li Gun and Jong Yun-Hyong, Director of the Flood Damage Rehabilitation Committee (FDRC). We advised North Korean officials that the U.S. Senate would be considering legislation later this year related to human rights conditions in North Korea and that deep concern exists regarding human rights abuses inside North Korea. The staff delegation also expressed concern about the status of North Korean refugees in China and the harsh treatment they sometimes receive upon returning to North Korea. We noted China's unwillingness to establish a formal structure of assistance for refugees, and urged North Korean officials to cooperate with NGOs and other members of the international community seeking to address the humanitarian needs of this vulnerable population. Given Kim Gye-gwan's initial willingness to engage in discussions on this sensitive issue, the question of DPRK prisons and the conditions under which prisoners are held should be a matter for future discussions involving the United States and other countries.

Economic Reforms

North Korea launched a major economic reform initiative on July 1, 2002. These reforms hold both promise and peril for the North Korean people generally and for the regime of Kim Jong-il. The government of North Korea has taken several steps to implement the reforms. Moreover, officials with whom we met recognize and acknowledge that North Korea's economic performance is ultimately tied to the peaceful resolution of the nuclear crisis.

Background

The main goals of the North's economic reform initiative are to boost production and improve living standards by introducing agricultural price incentives and stimulating the production of light industrial goods. The first step of the reform process emphasized raising wages and commodities prices to increase food production and decrease dependence on foreign aid. Subsequent reforms include new laws governing foreign investment and trade and a renewed emphasis on the development of three special economic zones -- Sinuiju along the Chinese border, Naja-Sonbong on the east coast, and Kaesong Industrial Park, a joint venture with Hyundai located close to the DMZ and Seoul.

The 2002 reforms built on earlier initiatives – notably the 1998 Constitutional revision which for the first time recognized private ownership of “income obtained through legal economic activities” – while introducing several new concepts. Farmer income is now linked more closely to production, and small private plots are allowed to be planted alongside those plots allocated to state-directed food production. The state has taken steps to re-zone small plots into larger, more efficient plots, and introduced a variety of new seed technology and fertilizers. Similar initiatives in the industrial sector allow factories to shift production of goods once state quotas have been met -- a kind of dual track system similar to that tried by China 30 years ago. Although ostensibly able to pursue new production, factories have no obvious source of capital for inputs, and they must still apparently maintain bloated work forces. In short, North Korea's antiquated industrial base is not well positioned to meet consumer demand for light industrial

products.

It is not clear how much productive capacity will be freed up by reforms, or indeed, if North Korea's industrial sector is capable of producing items North Korean consumers want absent a significant injection of capital and know-how. New small, family-size business are beginning to provide services and produce goods, but it remains unclear whether these grass-roots initiatives can compensate for the lack of productivity from large, state-owned factories that remain under utilized and largely dormant.

For years, China has tried to encourage North Korea to follow its model of market socialism, but Pyongyang has proven reluctant, constrained by national pride and the *juche* (self reliance, independence) political philosophy. Since the launching of the July, 2002 economic reforms, however, DPRK officials have begun to study China's success more closely. But even as it begins to embrace market principles, the North's economic prospects remain hampered by resource constraints. The North suffers from chronic shortages of electricity, food, material resources (especially timber and coal), capital, technology, and trained administrative personnel. These constraints serve as a break on the pace of economic growth. The net result is a reform package that remains inchoate, but nonetheless significant.

Markets Sprout

Perhaps the most significant aspect of the July 2002 economic reform package was the introduction of "general markets" at which farmers could sell their produce and craftsman could sell their wares. Until recently, these markets have been rather rudimentary, consisting of large open-air stalls enclosed by some kind of fencing, and they have been strictly off limits to foreigners. That is changing. Farmers markets are evolving into general markets. In recent months, the North has taken the concept of the market to its next logical evolution -- a large, covered, regulated market, complete with foreign exchange service, a café, and a wide variety of both domestic and imported consumer goods. The "fire wall" that used to separate markets for food and markets for goods has been breached.

We visited Pyongyang's "flagship" general market: the Tong-il Street Market. ***It must be noted that the Tong-il Street market is not typical, and that Pyongyang as a whole is not representative of conditions elsewhere in North Korea. Therefore, one cannot draw conclusions about market conditions throughout North Korea based only on a visit to one market in Pyongyang. That said, the Tong-il Street market, completed last summer, appears to be in the vanguard of market reform in North Korea, and was presented to the delegation as a clear indication of where North Korea wants to go.***

The Tong-il Street Market has more than 500 vendors, each renting stall space from the Tong-il Street Market for 80 won a day (about \$3 month). Vendors sell a huge variety of food imported from China, including pineapple, bananas, and melons. They also sell Fuji apples from Japan – seven for one dollar – and Russian vodka. In addition to food, shoppers can find clothing, shoes, consumer electronics, major appliances, furniture, artwork, etc.

Unlike the markets set aside for senior Korean Workers Party officials, the Tong-il Street Market appears to be open to the general public. There are no ID checks and no armed security guards. The market was bustling when we visited. Pyongyang residents typically tend to be a better off than residents of other parts of the country, but given the prices for most goods, there is no reason to believe that similar markets would not attract shoppers elsewhere in urban North Korea. We saw vendors accepting a variety of currencies – Chinese Renminbi, Japanese Yen, American Dollar, Euros – and gladly taking the opportunity to negotiate a favorable exchange rate with an unwary shopper. Vendors appeared to have the ability to provide change in several currencies. One dollar traded for 1,000 DPRK Won at the stalls, slightly above the official rate of 900 Won/dollar, but below the “floating” black market rate of roughly 1,200 Won/dollar. Vendors bargained with enthusiasm and exhibited considerable entrepreneurial spirit.

Are these kinds of markets the future for North Korea? It is too soon to say. The Tong-il Street market was opened last August, and plans call for similar markets to be constructed in each of Pyongyang’s 21 districts and then throughout the country. These covered, climate-controlled markets are intended gradually to replace the open-air markets that continue to cater to buyers with more limited income. Large markets are part of the story of North Korea’s market reform initiative. In Pyongyang, we also observed new small vendor stalls launched since last summer. We saw similar stalls last summer in Nampo and in Yongbyon city this year. These street stalls, selling a variety of small snacks, cigarettes, and liquor, appear popular, and have grown steadily in number over the past two years. For the first time, we were able to make a purchase at one of these street stalls -- five Chinese chocolate bars for a dollar. The vendor smiled as she took our one dollar bill, but also seemed a bit wary of making a sale to a foreigner.

Economic Prospects

North Korea has a shortage of economic expertise at all levels of government, but is beginning to take steps to remedy that deficiency. Interestingly, China has begun training programs for DPRK economic officials under the auspices of the Chinese Academy of Social Sciences. Chinese officials and think tank specialists report a new willingness on the part of their DPRK counterparts to learn from China’s experiences with economic reform and the privatization of state-owned enterprises.

North Korea’s economic reforms are not without risk. In the short run, price adjustments could increase inequality and exacerbate existing social differentiation. North Korea has long maintained an elaborate system of preferences, and the “haves” are now even more distant from the “have nots.” Inflation has also become a major concern. Some initiatives – such as a zero interest 10-year bond with lucky lottery winners eligible for “bonus interest” – at first blush seem ill-considered or downright Orwellian. However, bonds could in the long run provide a vehicle for privatizing state assets through debt-equity swaps as occurred in the former Soviet Union.

If North Korea is able to stimulate agricultural production and create functioning markets, it may not be enough to turn around its ailing economy. North Korea is primarily an

industrial society, with roughly 70 percent of the population residing in cities. Building a viable light industrial sector in North Korea and making obsolete heavy industries productive will require major restructuring and large infusions of capital and technology.

In sum, reforms in North Korea may create as many “losers” as “winners,” at least in the short run, and this could eventually undermine social stability. Reforms designed to boost commodity prices may be good for farmers and those with access to hard currency, but for urban dwellers on fixed income, the price increases for food and the devaluation of the North Korean Won against the dollar exact a heavy toll. The Won has gone from 150 Won/dollar in 2002 to 900 Won/dollar in October, 2003, with unofficial “black market” rates reaching as high as 1200 Won/dollar. The state seems aware of this problem, and has boosted salaries for miners and members of the armed forces – presumably two sectors of the work force the government must keep happy to avoid major unrest.

While it is too soon to judge whether North Korea’s economic reforms will kick-start its economy, there is no doubt that the state is committed to the reforms and is pursuing them with gusto. Success may depend in large measure on whether North Korea can solve the nuclear crisis and gain access to foreign capital, investment, and trade.

Beijing, Seoul and Tokyo

Upon departing Pyongyang and en route back to the United States, we met with U.S. and respective country officials in China, South Korea, and Japan to answer questions regarding details of our visit to the DPRK. While all the parties to the six party talks share the goal of a non-nuclear Korean Peninsula, each nation brings its own priorities to the talks. Officials in Beijing, Seoul, and Tokyo, each shared their country’s particular concerns with the staff delegation. We gained a deeper appreciation for the special responsibility China feels as host and facilitator of the talks, and were reminded of the priority Seoul attaches to the maintenance of peace and stability on the peninsula as this diplomatic process moves forward. In Tokyo, we gained insights into the incredibly important issue of the abductees, and how it informs Japanese policy making as Tokyo participates in the talks.

Conclusions/Key Findings

- 1) DPRK officials believe the United States will launch a pre-emptive attack on their country.
- 2) North Korea has restarted its Yongbyon nuclear reactor which has the potential to produce 5-6 kilograms of plutonium per year. The North could at any time easily reprocess spent fuel from the reactor to harvest plutonium for use in nuclear bombs.

- 3) North Korea is in the midst of a significant economic reform movement, the full implications of which remain to be seen. North Koreans intimately involved with the reform initiatives appear to be among those in the DPRK pushing the hardest for resolution of the nuclear issue.
- 4) DPRK officials are interested in reducing the nation's dependence on food aid and want outside help developing a more productive agriculture sector.
- 5) Eliminating North Korea's gulags and addressing the humanitarian needs of North Korea's prison population should become a priority for the United States government and the entire international community.
- 6) Significant communications and coordination problems continue to hamper the six party talks. *The talks are more likely to make progress if multi-party working groups are established to define terms, discuss verification protocols, and exchange views on how any deal might be phased.*
- 7) China and South Korea place a premium on maintaining peace and stability on the Korean Peninsula. *Both seem prepared to go to great lengths to avoid either a war on the peninsula or an abrupt collapse of the Kim Jong-il regime.*
- 8) China, on whom we rely as key facilitator in the six-party talks, shares our goal of a non-nuclear Korean Peninsula. *Nonetheless, China will always place its own interests first in this process, and Beijing's interests are not identical to our own.* DPRK officials are not certain that China has accurately transmitted messages between Washington and Pyongyang.

Key Interlocutors Include the Following:

People's Republic of China

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Political Counselor
U.S. Embassy

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Political Officer
U.S. Embassy

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Xia Jihui
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