

# **A South Korean Perspective on the Impact of Sanctions**

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There is no way to hurt the regime of the DPRK without hurting its people; and there is no way to support the people of the DPRK without supporting its regime. Thus, discussing the effectiveness of sanctions against North Korea demands hard labor in fact-finding and tremendous patience until the desired effects are witnessed. Sanctions are time and energy consuming. In order to curb North Korea's enthusiasm for long-range missiles and nuclear weapons, the sanctions regime needs to be upgraded.

Smart sanctions were not as smart as imagined because of their two-sided effects – inflicting suffering on the people of the target country and simultaneously augmenting the rationale for harsher oppression by the leadership of the target country. As former UN Secretary-General Boutros Boutros-Ghali described it, economic sanctions seem to raise an ethical question of “whether suffering inflicted on vulnerable groups in the target country is a legitimate means of exerting pressure on political leaders whose behavior is unlikely to be affected by the plight of their subjects.”<sup>1</sup> UN sanctions on targets such as South Africa in the 1980s and Iraq in 1991 were accompanied by a negative humanitarian impact.

Smart sanctions are designed to effectively put direct pressure on individual national policymakers. As David Baldwin argues, smart sanctions are deemed effective as long as they create costs that are a critical factor in the calculus of decision-making by the target state.<sup>2</sup> Their purposes include symbolism and expression of disapproval, and persuading the targeted state to change its practices.<sup>3</sup> Smartly targeted sanctions include arms embargoes, financial sanctions on the assets of individuals and companies, travel restrictions on the leaders of a sanctioned state, and trade sanctions on particular goods.

The first endeavor to focus the penalty more directly on those most responsible for the crisis brought together key academics, government officials, UN practitioners, and banking officials in New York in 1998. This initial discussion of the feasibility of targeted financial sanctions was facilitated by the Swiss government that launched the Interlaken Process in 1998. The banking industry, already equipped with the tools for dealing with money laundering, began to play a major role in further sanctioning.

The most conspicuous case of financial sanctions on North Korea is the sanctioning of Banco Delta Asia (BDA) in Macao in 2005, where \$25 million of North Korean funds distributed across 52 accounts was frozen. In response to international pressure, North Korea actually took additional measures toward denuclearization. Thus, the conclusion of the BDA ruling was that financial sanctions could hit North Korea where it hurt.<sup>4</sup> However, the North Koreans, who learned a lesson from the BDA case, started improvising alternatives to the conventional use of official transaction systems.

To make smart sanctions work, China's cooperation is necessary. Trade between China and North Korea has continued to increase since 2000, serving as a lifeline through which hard currency as well as necessary goods are provided to the North Korean leadership. A recent report of China's alleged decision to close the Foreign Trade Bank of the Democratic People's Republic of Korea's accounts in Chinese banks is not enough to indicate its willingness to support world efforts to sanction North Korea.

North Korea's demand for hard currency seems to be greater than ever. Under the hereditary leadership of a young Kim, the ambition to build a new “Kimdom” (Kim's Dominion)

requires a bigger inflow of hard currency. The Pyongyang regime openly advertises to the world its multiple projects such as a ski resort, tourist programs, and newly designated special economic zones. Away from the stage of its serial provocations, the Kim Jong-un regime is shifting its focus toward the next stage of strategic conciliation and cooperation with the international community. It is the right time for the smart sanctions regime to refine its efforts. The South Korean government is determined not to allow the North Korean regime to take advantage of the world's open financial system for illicit purposes.

Over the past ten years, the impoverished North Korean regime has conducted five nuclear tests, inviting multilateral and bilateral sanctions. Each time sanctions were upgraded, they were "hailed as the most 'comprehensive,' 'robust,' and 'unyielding' sanctions to date against North Korea's pariah government.<sup>5</sup> However, because previous rounds of sanctions failed to curb Pyongyang's drive to advance its nuclear weapons program, the effectiveness of additional punitive economic measures are still doubted.

As long as Pyongyang's provocations cannot be stopped, the historical pattern renews skepticism about whether the world's harmonizing acts against North Korea will ever have a measurable impact. In particular, if nuclear weapons are not optional but essential for the regime's survival, the impact of any kind of sanctions will be limited. Since North Korea's economy has been essentially bankrupt for several decades, the impact of sanctions is further limited. Heightened tensions and isolation deepened by harsher sanctions help the Pyongyang regime control the redistribution of resources to any individuals who could be potential rivals to the Kim leadership.

Optimists may say that the desired effect of sanctions can be produced some time in the future if a few critical conditions are met, e.g., having enough time for increased cooperation with China to willingly enforce the sanctions. However, the reality is not like a well-designed laboratory for an ambitious experiment. The participating countries' interests and positions are different and, even if consensus were reached, their partnership is fragile.

During the years when North Korea devoted all of its energy to the development of nuclear weapons, causing the sanctions to be harsher, its economy ironically became more stable.

Many question how this rogue regime with a malfunctioning planned economy could survive global pressure. In this regard, the purpose of this chapter is to review the background of sanctions against North Korea and to discuss their effectiveness. This academic exercise is aimed at contributing to efforts at making North Korean behavior change in an acceptable way.

## SANCTIONS AGAINST NORTH KOREA

The North Korean regime's efforts to acquire weapons of mass destruction (WMD) increase the unpredictability and instability of international relations that have been secured under the nonproliferation regime. Because of the unimaginable brutality of nuclear and chemical weapons, nations accepted an international system that put those weapons only in the hands of a few powers. The global community has not been persuaded that the isolated, totalitarian regime in North Korea would be committed to the preservation of world peace if it were to be granted the status of a nuclear power.

North Korea has a track record of systematic violations of universally recognized human rights norms. In February 2017, the assassination of Kim Jong-nam, the half brother of Kim Jong-un, brought world condemnation against the North Korean regime, whose legitimacy is based on a third-generation inheritance of power. The regime mobilized its diplomats and dispatched workers to commit the crime by using the internationally banned chemical VX. In addition, laborers dispatched abroad are exploited to earn hard currency to support the dictatorial leadership.

### Multilateral Sanctions by the UN Security Council

As shown in Table 1, there are a number of resolutions the UN Security Council (UNSC) has adopted, particularly since North Korea's first nuclear test in 2006. Resolution 1718 in 2006 demanded it cease nuclear testing and prohibited the export of some military supplies and luxury goods to North Korea. Resolution 1874, adopted in response to the second nuclear test in 2009, embargoed North Korea's arms trade and requested UN member states to inspect North Korean ships suspected of carrying material related to the nuclear weapons program.

Resolution 2087, passed in 2013 after North Korea's long-range ballistic missile launch the previous year, augmented measures to seize any of its cargo ships suspected of involvement in WMD programs. Resolution 2094, in response to North Korea's third nuclear test, focused on financial sanctions, including shutting North Korea out of the international financial system. Resolution 2274, adopted after North Korea's fourth nuclear test and another rocket launch, banned North Korea's export of coal, iron, gold, rare earth metals, etc., with exemptions for livelihood purposes. Resolution 2321, passed after its fifth nuclear test, added to the list of banned exports items such as copper, nickel, zinc, and silver, as well as capping the maximum amount of North Korean exports of coal.

In theory, UNSC sanctions have evolved to increase the pain the North Korean leadership feels. In reality, however, the greater the pain inflicted by the sanctions, the bigger the scale of provocations. Continued efforts to magnify the impact of UN sanctions have failed to curb North Korea's continued efforts to improve its nuclear capabilities.

**Table 1. UNSC Resolutions (UNSCR) Regarding North Korea**

NK Actions	UN Reactions	Main Features
1st Nuclear test (Oct 9, 2006)	UNSCR 1718 (Oct 14, 2006)	<ul style="list-style-type: none"> <li>• Demands that North Korea cease nuclear testing</li> <li>• Prohibits the export to North Korea of military supplies and luxury goods</li> </ul>
2nd Nuclear test (May 5, 2009)	UNSCR 1874 (Jun 12, 2009)	<ul style="list-style-type: none"> <li>• Broadens arms embargo</li> <li>• Encourages states to inspect ships and destroy and cargo suspected to be related to WMD</li> </ul>
Missile (Dec 12, 2012)	UNSCR 2087 (Jan 22, 2013)	<ul style="list-style-type: none"> <li>• Clarifies states' right to seize and destroy WMD-related cargo to or from North Korea</li> </ul>
3rd Nuclear test (Feb 12, 2013)	UNSCR 2094 (Mar 7, 2013)	<ul style="list-style-type: none"> <li>• Puts sanctions on money transfers</li> <li>• Shuts North Korea out of financial system</li> </ul>
4th Nuclear test (Jan 6, 2016 and missile (Feb 7, 2016)	UNSCR 2270 (Nov 30, 2016)	<ul style="list-style-type: none"> <li>• Bans exports of coal, iron, gold, rare earth metals, etc., with exemption for livelihood purposes</li> </ul>
5th Nuclear test (Sept 9, 2016)	UNSCR 2321 (Nov 30, 2016)	<ul style="list-style-type: none"> <li>• Caps North Korea's coal exports</li> <li>• Bans its exports of copper, nickel, zinc, silver</li> </ul>

\* Exact dates depend on the location of the action

## UNILATERAL U.S. SANCTIONS

As shown in Table 2, U.S. administrations have issued executive orders to address the threat from North Korea’s development of nuclear weapons and to introduce measures to stop its bad behavior. Executive orders have been made possible on the basis of the U.S. Constitution and laws including the National Emergencies Act, the International Emergency Economic Powers Act, the Trading with the Enemy Act (TWEA), and the Arms Control Act.

Executive Order 13466 was issued in June 2008 when negotiations with North Korea on denuclearization appeared to have reached the final stage. It addressed the seriousness of the possible proliferation of nuclear materials or technology. In August 2010, when North Korea’s attack on the *Cheonan* heightened tensions on the Korean Peninsula, U.S. Executive Order 13551 designated North Korean persons as sanctions targets and banned the trade of North Korean arms and the sale of luxury goods to North Korea.

Executive Order 13570, issued in April 2011, when tensions were heightened after the North Korean shelling of Yeonpyong Island in November 2010, banned the importation of any goods, services, or technology from North Korea. Executive Order 13687 was issued in January 2015 with regards to North Korea’s hacking of Sony Pictures two months prior. It blocked the property of the North Korean government or the Workers’ Party of Korea, which became designated entities in U.S. sanctions for the first time.

Executive Order 13722, issued in March 2016 in response to the fifth nuclear test and another missile launch, blocked the property of any U.S. person who is involved with North Korean industries, including transportation and mining, cyber attacks, human rights abuses, censorship, and exportation of North Korean workers. Also, it banned the exportation or re-exportation of goods, services, or technology to North Korea, and prohibited new investment in North Korea by U.S. persons.

NK Actions	UN Reactions	Main Features
Working on denuclearizing NK	13466 (Jun 26, 2008)	<ul style="list-style-type: none"> <li>Freezes North Korean property in the U.S.</li> <li>Stops U.S. persons from registering a vessel in NK or operating any of its flagged vessels</li> </ul>
2009 test of nuclear device and missile & 2010 attack on SK navy ship	13221 (Aug 30, 2010)	<ul style="list-style-type: none"> <li>Blocks designated NK persons’ property</li> <li>Bans the trade of NK arms and its material; luxury goods; illicit economic activity</li> </ul>
Tension heightened since Nov 2010 Yeonpyong shelling	13570 (Apr 18, 2011)	<ul style="list-style-type: none"> <li>Bans the importation into the U.S. of any goods, services, or technology from NK</li> </ul>
Hacking of Sony Pictures in Nov 2014	13687 (Jan 2, 2015)	<ul style="list-style-type: none"> <li>Blocks the property of NK Government or the Worker’s Party of Korea</li> </ul>
2016 test of nuclear device and missile launch	13722 (Mar 15, 2016)	<ul style="list-style-type: none"> <li>Blocks the property of any U.S. person who is involved with NK industries such as transportation and mining, cyber attacks, human rights abuses, censorship, exportation of NK workers</li> <li>Bans the exportation or re-exportation of goods, services, or technology to NK</li> <li>Prohibits new investment in North Korea by U.S. persons</li> </ul>

\* Previous Executive Orders include 12938 (1994), 13094 (1998), 13382 (2005).

Besides Executive Orders, on March 31, 2017, the U.S. Department of the Treasury also sanctioned eleven individuals and one entity associated with providing funding and support for North Korea's WMD program. The Trump administration seeks to close down more procurement channels and funding sources for North Korea in third party countries, including China, Russia, Vietnam, and Cuba.<sup>6</sup>

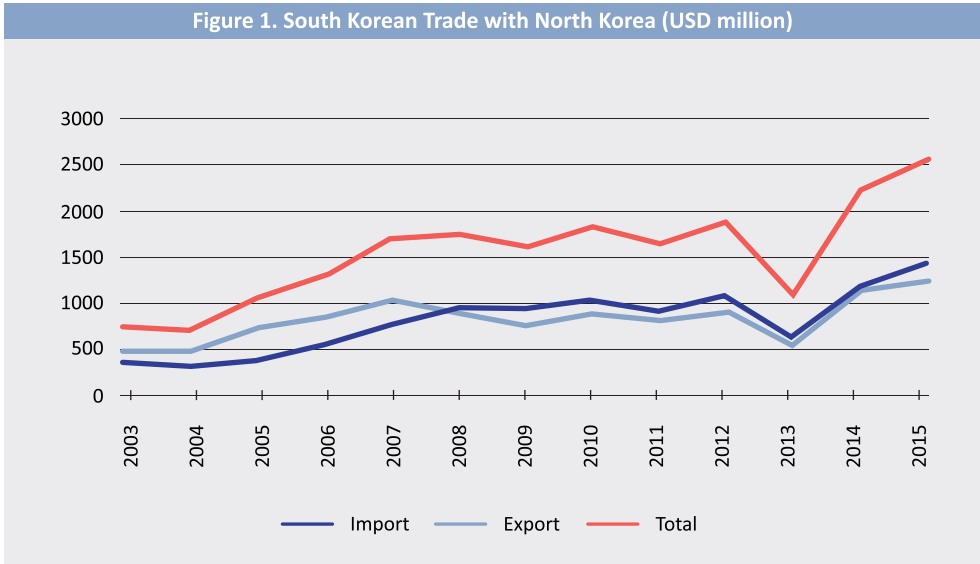
### **Inter-Korean Relations and Sanctions Effectiveness**

South Korea has initiated and supported global efforts to punish North Korea for its bad behavior. Not only has it been diligent in implementing whatever is stipulated in the UNSC resolutions, it has taken unilateral sanctions measures against North Korea, seen in the shutdown of the ten-year-old Kaesong Industrial Complex (KIC) immediately after the fourth nuclear test in February 2016. Stopping the KIC was a reaction to the North Korean regime's contradictory policy of pursuing WMD on the one hand and of national reconciliation on the other. What triggered the South Korean government to shut down the KIC in 2016? What was the main purpose of the shutdown? What was the essence of the cost-benefit calculation by South Korean decision makers?

The main argument in support of the KIC shutdown is that payments of labor wages were used to contribute to the development of nuclear weapons programs in North Korea. The South Korean leadership at the time justified its decision to stop business operations in the KIC, expressing confidence in the close connection between business and provocations.<sup>7</sup> Some criticize the closure as "shooting oneself in the foot" because North Korea's nuclear ambitions could not be stopped by doing this,<sup>8</sup> and South Korean firms were the ones that were hurt.

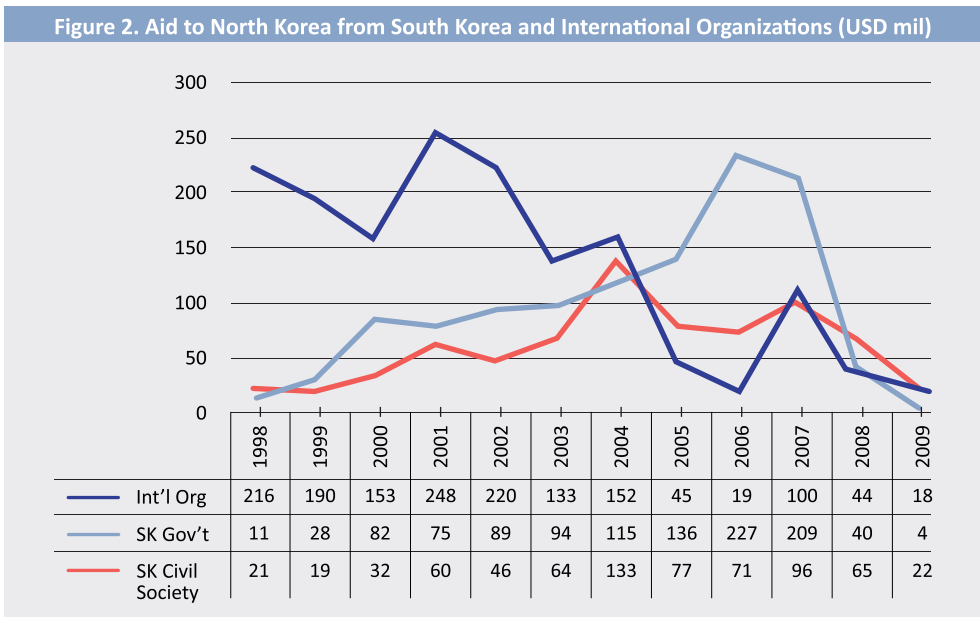
An annual income of \$100 million from the KIC may be meaningful for North Korea, whose options for acquiring hard currency are quite limited. Stopping the money inflow seems to have not influenced the North Korean regime, whose main interest is not the growth of people's wealth but the growth of the regime's destructive power. This criticism points out that there is little benefit South Korea could gain from the closure of the KIC. Through projects in Kaesong, South Korean businesses enjoyed a monopoly augmented by direct and indirect government subsidies and the exploitation of cheap North Korean labor. Thus, it is argued that the closure of the KIC hurt the South far more than the North.

North Korea experienced the sudden administrative cost of relocating the 54,000 well-trained Kaesong workers as well as the loss of their regular income. Despite losing the income from the KIC, the Kim Jong-un regime continued to develop its nuclear weapons with its fifth nuclear test in September 2016, indicating the limited effectiveness of South Korean sanctions. The efforts to upgrade sanctions ended up stopping business cooperation between the two Koreas. As shown in Figure 1, inter-Korean trade had steadily increased until early 2016, even after it was reshaped due to the North Korean attack on a South Korean naval ship in 2010, when the South Korean government adopted bilateral sanctions blocking all exchanges and business cooperation except the activities in the KIC. Thus, since 2010, inter-Korean trade has consisted only of transactions through the KIC.



Source: Korean Ministry of Unification

As shown in Figure 2, international organizations’ aid to North Korea peaked in 1998-2000 and then continued to shrink. Since inter-Korean political relations turned positive in 1998 when the Kim Dae-jung administration’s Sunshine Policy was introduced, South Korean NGOs actively engaged in inter-Korean reconciliation and cooperation programs and projects. However, after some trial and error, South Korean civil society’s interest in aiding North Korea began to diminish from 2004 when the KIC was launched. The focus of South Korea’s approach to the North shifted from humanitarian assistance to business cooperation, and aid to North Korea was initiated mainly by the South Korean government until 2009 when the North conducted its second nuclear test.

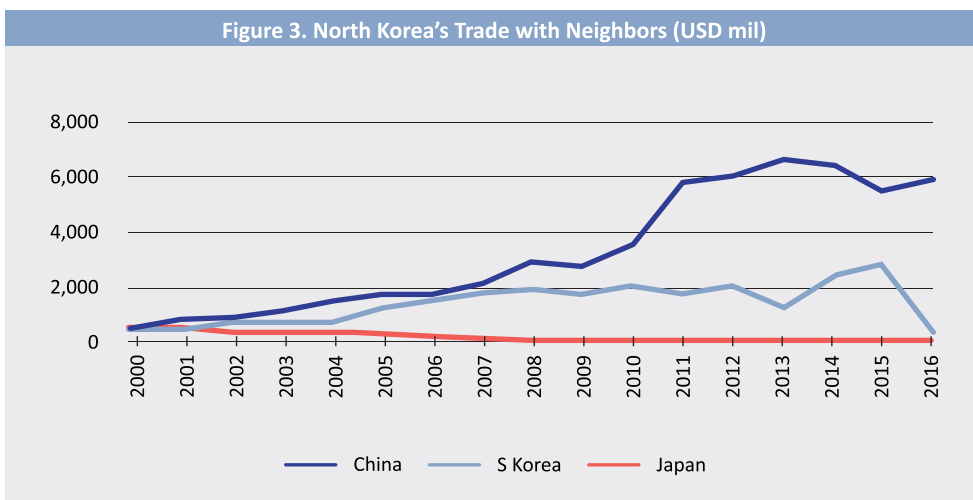


Source: Korean Ministry of Unification

In sum, multilateral and bilateral sanctions on North Korea triggered by North Korean bad behavior have decreased inter-Korean cooperation. The Pyongyang regime is now further isolated and losing any chance to figure out an alternative to its costly weapons development programs. So far, sanctions have not made the North restore dialogue with the South.

## NORTH KOREA-CHINA RELATIONS AND SANCTIONS EFFECTIVENESS

The Chinese government is quite determined to implement UNSC sanctions measures against North Korea for its violation of international laws and agreements regarding WMDs. As a traditional ally and close neighbor of North Korea, however, China has a policy dilemma. Geopolitics give China pause with regard to strategic calculations of the relationship with North Korea in light of China's past and future national interests. As a globally influential player, China clearly understands the importance of punishing North Korea, a violator of international agreements. However, as an ideologically bonded ally, it cannot push North Korea into a corner, where its fragile economy may collapse. China's active engagement with the North Korean economy is now threatened by escalated provocations that result in stronger demand for tougher sanctions against North Korea.



Source: Korea International Trade Association (KITA) & China Customs Statistics

Figure 3 shows the trend of North Korea's trade with its close neighbors China, South Korea, and Japan. Japan was an equal shareholder in trade with North Korea in 2000 when North Korean trade with China, Japan, and South Korea recorded \$488 million, \$464 million, and \$425 million, respectively.<sup>9</sup> From 2000, trade between North Korea and China showed an average growth of 22.4 percent annually, except in 2009 and 2014. The superficial decrease in 2009 from the previous year was 38.6 percent, but the substantial decrease was only 4.2 percent. Trade in 2014 showed a decrease of 2.8 percent compared to the previous year, but it actually increased by 4.9 percent if invisible imports of strategic materials such as oil are considered.<sup>10</sup>

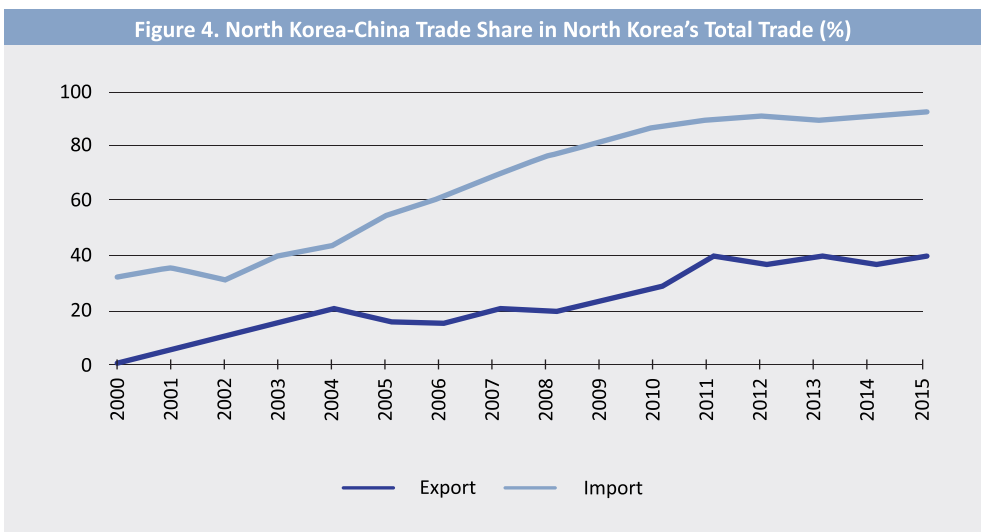
Since China joined the World Trade Organization (WTO) in 2001, it has aggressively expanded its influence by increasing trade and investment, including with bordering states such as Mongolia and North Korea. In particular, since 2010, when China renewed its national economic



development projects, trade with North Korea began to soar even while North Korea’s political environment was deteriorating at a rapid pace, exemplified by the North Korean attacks on the *Cheonan* and on Yeonpyong Island.

As the speed of inter-Korean economic cooperation fell from 2008, North Korean dependency on the Chinese economy proportionally increased. Kim Jong-il had visited China to discuss how to receive aid in the form of economic cooperation. North Korea was interested in building economic infrastructure to surf the prospective wave from the latest Northeast China revitalization plan.<sup>11</sup>

Trade between North Korea and China has been influenced by changes in both politics and the market. When bilateral trade shrank for a time, the effect of sanctions was not a unique factor. Their trade has also reflected a decline in the export price of coal or a decrease in Chinese energy consumption, for example, during 2014-2015. This explanation is supported by other cases, including Mongolia’s trade with China.



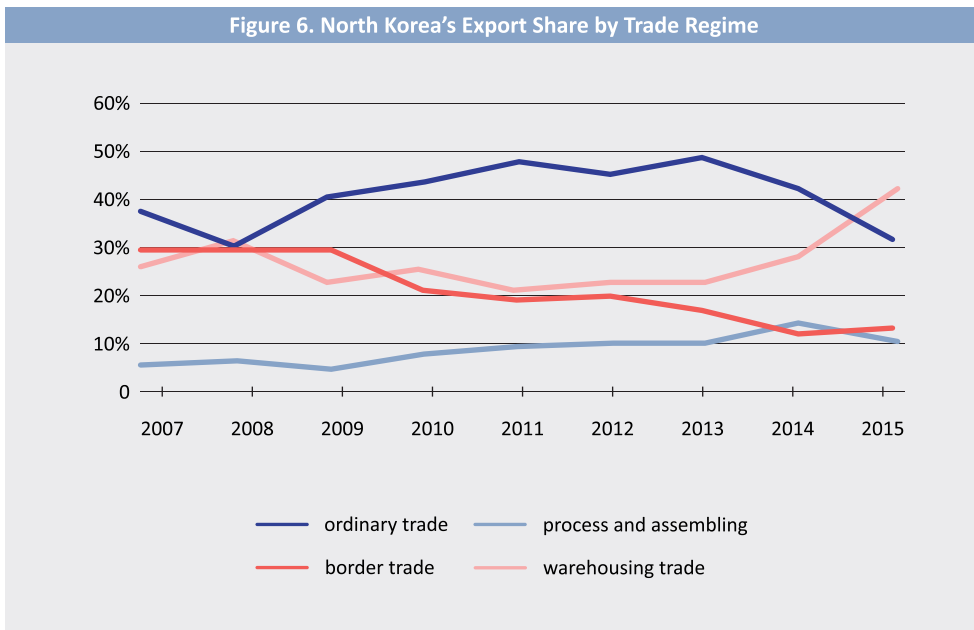
Source: KITA and UN Comtrade Database

Figures 4 and 5 support the argument that the continued increase in China’s trade with its neighbors North Korea and Mongolia has reflected synchronized supply and demand. The share of Mongolia’s exports to China in its total exports soared to almost 90 percent in 2014, whereas the share of North Korea’s imports from China in its total imports passed 90 percent in the same year. In this regard, the increased demand for tougher sanctions on North Korea has brought bigger attention to the waxing trade between North Korea and China.

The year 2015 was the first bilateral trade decrease since 2009. According to China customs, trade with North Korea was \$5.4 billion in 2015, a drop of 14.7 percent from \$6.4 billion in 2014. North Korea’s exports to China in 2015 recorded \$2.5 billion, 12.6 percent lower than \$2.8 billion in 2014. Its imports from China marked \$2.9 billion, a decrease by 16.4 percent from \$3.5 billion in 2014. These numbers reflect structural changes, such as the lowering of China’s GDP growth rate or the shift of focus from export-driven to domestic consumption-driven growth.

During 2014-2015, North Korea’s imports declined, probably related to a shortage of foreign currency due to export reductions or economic sanctions. Alternatively, it may be part of the consequences of domestic change in response to outside pressure. Pyongyang’s new propaganda insists that production capabilities have improved and more domestic goods are available, which is opposite to the reality, where North Korea is disconnected from global sources of hard currency.

Some strategically spotlighted industries of North Korea, however, tend to show positive change. For example, the increase in coal exports to China implies that North Korea has improved its mining capability, by either upgrading its production system or receiving more foreign investment. As shown in Figure 6, in 2015 warehousing trade surpassed ordinary trade. Warehousing trade is suspected of being detour trade from North Korea to third countries, via China.<sup>12</sup> It primarily consists of processed goods, including textiles, rather than raw materials. Thus, it can be presumed that North Korea has improved its production capacity in manufacturing, which made a notable contribution to the expansion of trade.



Source: China Customs Statistics

In early 2016, North Korea's trade with China was expected to be affected by many factors including new economic sanctions, the shutdown of the KIC, a continued decrease in raw material prices in the international commodity market, and China's import decline. However, there was an increase. Exports to China in 2016 reached \$2.6 billion, an increase of 6.1 percent from the previous year, led by coal (\$1.1 billion), fabrics (\$600 million) and iron ore (\$200 million). In 2016, total Chinese imports of North Korean coal were around \$1.1 billion, an increase of 12.5 percent from the previous year. And in the first two months of this year, Chinese imports of North Korean coal had already reached 2.69 million metric tons equivalent to \$219.5 million, representing over 50 percent of the \$400.8 million limit mandated by the UNSCR 2321 for China's 2017 imports of coal from North Korea.

## CONCLUSION

Economic sanctions against North Korea have been imposed by the United States and the United Nations since the armistice treaty signed in 1953. Since 2006, when North Korea's first nuclear test occurred, more significant sanctions were introduced. Pyongyang has displayed its nuclear and ballistic missile capabilities, violating international laws and norms and threatening the United States specifically. On the first day of 2017, Kim Jong-un declared that his state had reached the final stage of being capable of launching an inter-continental ballistic missile (ICBM), undoubtedly targeting the continental United States, which he may be able to reach in the near future. In the 21st century, North Korea appears to be unique in continuing its nuclear build-up despite increased pressure from the international community. Thus, it is said that coercive diplomacy has failed.

Upon his first official visit to East Asia in March 2017, U.S. secretary of state Rex Tillerson admitted that approaches to the North Korean nuclear problem have proved to be a failure over the past twenty years. For the last ten years of global economic sanctions, the world has witnessed five nuclear tests. The reasons for the failure of costly efforts to make sanctions on North Korea effective include a weakening global "united front." China is regarded as exploiting loopholes.<sup>13</sup> Its enforcement is the key to effective sanctions.

For the past decade at least, China is said to have turned a blind eye to sanctions violators and kept the non-compliant North Korean regime alive. The United States blames China for its reluctance to use leverage over North Korea, while China blames the United States for its reluctance to open an unconditional dialogue with North Korea. For the United States, sanctioning North Korea is regarded as an inevitable choice to keep international peace and order from a rogue nation's irrational behavior. However, for China, the same action may be interpreted as weakening the traditional socialist alliance with North Korea. The two big powers' tug-of-war over the North Korea problem ironically provides North Korea with strategic room to manipulate the crisis situation.

North Korea's fourth nuclear test in February 2016 triggered South Korea's decision to introduce THAAD. The Park Geun-hye government officially announced in July its decision to put THAAD in a southeastern area of South Korea. In response to that decision, China began to "retaliate" against South Korean businesses to pressure the South Korean government.<sup>14</sup> In the eyes of the Chinese leadership, North Korea's obsession with WMDs may be tolerable, whereas South Korean accession to its ally's

additional self-defense measures, including the installation of THAAD on Korean soil, is provocative. China's admonishment with no punishment has spoiled the North Korean regime.

The effectiveness of sanctions depends on whether the United States and China have a common understanding of the threat from North Korea. Some now contend that China views North Korea's nuclear ambitions as a threat not only to the U.S., ROK, and Japan's interests and security, but also to Chinese interests and security.<sup>15</sup> If this is true, it is a big shift.

The recent remark by Secretary of State Tillerson signaling the end of Obama's policy of "strategic patience" implies that the Trump administration will be active in considering a variety of policy options ranging from dialogue to military actions in solving the North Korea problem. However, during Obama's tenure, various options were already discussed as follows:<sup>16</sup>

- 1) Go to the United Nations Security Council
- 2) A "secondary boycott" on firms that do business with North Korea
- 3) Escalation: hit North Korea back
- 4) Strike a grand bargain
- 5) Pressure China
- 6) "Strategic patience" (otherwise known as containment)

Sanctions against North Korea have evolved; however, the reality is that North Korea's nuclear weapons program continues to develop. The same question is repeatedly asked: How can sanctions be upgraded to lead to a different outcome?

## ENDNOTES

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