

China-Korea Relations A Turning Point for China?

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This quarter marked a period of transition and tumult in China-Korea relations. Beijing revealed its own diplomatic initiative to settle the North Korean nuclear problem with a surprise announcement that it would host representatives from Pyongyang and Washington in multilateral talks. But that effort was set back by an embarrassing North Korean threat during the talks, warning that it had nuclear weapons and might test them in the near future. The economic and health threat from severe acute respiratory syndrome (SARS) was a major concern at the beginning of the quarter, but dissipated by the end of the quarter with little apparent lasting effect. South Korea's new Foreign Minister Yoon Young-kwan took his first trip to Beijing in April to meet newly installed counterpart Li Zhaoxing for the first of several meetings. The dates are now set for President Roh to follow in early July.

Despite the apparent volatility of events this quarter, however, there has been little apparent change either in the seriousness of the North Korean nuclear issue or in continued bullish prospects for buoyant China-Korean economic relations. Still, one can't help but feel that more volatility is on its way, and that tensions with North Korea will rise as events unfold in the second half of the year.

Beijing Hosts and Deals a Round of Nuclear Poker

The most difficult challenge in the high-stakes nuclear poker game between Washington and Pyongyang is finding the right venue and players to play their hands. Getting the key players to sit down at the same table is itself a significant diplomatic feat, and for the first time, Beijing hosted a round of talks that included both the United States and North Korea. The April 23-25 talks in Beijing were very exclusive. Only the hosts and key players from Washington and Pyongyang were allowed. South Korea, Japan, and Russia were excluded from this first round, but it turns out that there was no high-stakes dealing, no serious betting, and lots of bluff, so the other participants didn't miss any action at all. Washington said it wouldn't even play unless Pyongyang went all-or-nothing, and Pyongyang threatened to trump Washington with a nuclear test but refused to show any

of its cards – if indeed Pyongyang even had cards to play. In the end, with neither side willing to reveal its hand, the game was suspended for another day.

Going into the talks in Beijing, there were questions whether Beijing would simply be a host for a thinly disguised bilateral dialogue between representatives from Pyongyang and Washington or whether it would take an active role as a full participant in the dialogue. U.S. officials viewed Beijing as both active and constructive in its efforts to bring North Korea to the table and to reinforce to Pyongyang the dangers of pursuing a nuclear weapons program. However, North Korean delegation head Ri Gun delivered a clear message to Assistant Secretary of State James Kelly during a coffee break on the side of the meeting. Ri asserted that North Korea possessed nuclear weapons and might test or export them, while also offering further negotiations on the future of North Korea's nuclear program.

Ri's revelation was a shock to the United States and stung the Chinese precisely because President Hu Jintao only days earlier had tried to convince North Korean Gen. Cho Myung-rok, number two in the North Korean hierarchy, to end North Korea's pursuit of nuclear weapons. Cho was reportedly seeking assurances of China's assistance in the event of military hostilities, but to no avail. Ri's statement, coming after Hu's meeting with Cho, was interpreted as an embarrassing North Korean affront to China.

However, the fact that Beijing had taken steps to bring Washington and Pyongyang to the dialogue table was in and of itself a precedent-setting initiative. It showed that Beijing's new government recognized that it could not simply hide behind the old rhetoric of noninterference and peaceful coexistence if it really wanted to maintain regional stability and avoid the spectre of another Iraq in its own backyard. The "demonstration effect" of failed diplomacy leading to the U.S. military conflict with Iraq was probably additional motivation for China to stage talks with Washington and Pyongyang to avoid the consequences of failed diplomacy with North Korea. Certainly, Beijing could ill-afford the regional consequences of North Korea's nuclear program, including a likely chain reaction in which Japan, South Korea, and Taiwan may all consider possession of nuclear weapons necessary for their self-defense. So, the stakes for China are high, and the decision to host the talks helps to cement China as an indispensable player in matters concerning the future of the Korean Peninsula.

President Bush's persistent telephone diplomacy with Beijing had raised North Korea as an issue of importance in the U.S.-PRC relationship, and the leadership in Beijing has clearly recognized that there are limits to the losses that Beijing is willing to accept as a result of its past association with North Korea. Once viewed as a "strategic asset" and buffer that protected China from external threats, Chinese analysts increasingly view North Korea's instability, aggressiveness, and unpredictability as a "strategic liability." North Korea's willingness to surprise its hosts with its rude admissions that it had nuclear weapons and may test those caught leaders in Beijing off guard and further distanced Pyongyang from Beijing.

The end of the Beijing talks marked a new phase in U.S. multilateral diplomacy regarding North Korea, although the dates for a new round of talks, this time likely to include South Korea and Japan, remain unclear. Instead of responding directly to a North Korean dialogue proposal widely regarded as a nonstarter, the Bush administration has mounted a drive for international solidarity against North Korean nuclear weapons, which has included summits with ROK President Roh Moo-hyun and Japanese Prime Minister Koizumi Junichiro, Russian President Vladimir Putin, and a follow-up meeting with PRC President Hu in St. Petersburg prior to the Evian G-8 summit. U.S. efforts to persuade North Korea to include South Korea and Japan in the next round of talks with Pyongyang have been handled in close diplomatic consultation with the PRC. However, Beijing appears likely to be less cooperative with the U.S. at this time on a United Nations Security Council resolution condemning North Korea's violations of its nuclear commitments under the Nuclear Non-Proliferation Treaty (NPT) and International Atomic Energy Agency (IAEA). The expectation is that North Korea will eventually come to an expanded round of multilateral dialogue, although the extent of Beijing's cooperation to ratchet up pressure on Pyongyang remains unclear. China is balancing the value of enhanced cooperation with Washington and the danger that such a path may carry a real cost to China in the form of regional instability that might result from the collapse of North Korea. Bush administration expectations for China may exceed the price that Beijing is willing to pay in prodding North Korea in potentially dangerous directions.

Likewise, there is no public evidence thus far that Beijing is showing cooperation with the Bush administration's Proliferation Security Initiative, a multinational effort designed to strengthen interdiction of shipments of illegal or dangerous cargo, including drugs, missiles, or nuclear components. For such an effort to be truly effective against North Korea, Beijing's cooperation is essential, particularly in light of reports in the *JoongAng Ilbo* that North Korea may have shipped missile components to Iran by air in April and May. North Korean overflight of China to countries such as Iran greatly reduces the risk of interdiction in international waters or airspace, rendering potential application of the Proliferation Security Initiative to North Korea's most sensitive and destabilizing exports all the more difficult to enforce.

SARS: a Speedbump in Economic Relations

For all of the media talk about SARS and its potential impact on China's external economic ties, one might easily think that China's manufacturing and export engine might sputter, with potentially serious implications for the China-Korea economic relationship. But in the end, SARS only briefly cut the pace of growth of the relationship to a little over 30 percent year-on-year, rather than the over 60 percent growth achieved in the first quarter of the year. Exports from South Korea to China reached \$12.4 billion in the first five months of the year on the strength of continued rapid growth in exports of semiconductors, mobile phones, and computers. But the growth in exports to China slowed to 37.8 percent in May from over 57 percent in April as a result of the impact of SARS and a truckers' strike in South Korea. In the end, SARS was a mere speed bump on the road to an even more robust China-Korea economic relationship, delaying for the

time being China's rise in market share to surpass the United States as South Korea's number one export market. The United States was the destination for \$13.2 billion in exports during the five months of the year, a 0.7 percent increase from a year earlier.

The sector that took the biggest hit was the tourism and service industry, which suffered deep drops in passenger volume due to the SARS scare. Leisure travel to China dropped precipitously, replaced in part by the migration of Korean students who came back to Korea when schools were closed in early April in China due to SARS. Korea recorded its lowest monthly inbound tourist volume in seven years in May with only 265,204 visitors, a decline of 39.4 percent compared with the previous year. The number of Japanese and Chinese tourists to Korea was halved during this period. Likewise, the number of Korean outbound travelers dropped by 41 percent and 34.4 percent in April and May, respectively, with year-on-year declines for travel to China, Singapore, and Hong Kong of 60 to 70 percent.

According to a survey of 125 Korean firms conducted by the Korea Trade-Investment Promotion Agency, SARS related factory-slowdowns accounted for at least \$25 million in losses, a loss that if extrapolated to represent losses for all Korean operations in China could total \$2.5 billion in trade for the year. Korean businesses imposed restrictions on travel to China and required medical checkups, quarantines, and recent travelers to work at home for two weeks at the height of the epidemic. By the end of the quarter, however, most travel restrictions to China had been lifted and Korean executives flocked back to China to take care of business delayed at the height of the crisis. Business and leisure travel rates returned to their previous levels by the end of June. SARS was not enough to slow Shanghai in its quest to replace Pusan as the world's third busiest port in 2003. Although Pusan's 9.45 million twenty-foot equivalent units (TEU) volume in 2002 edged Shanghai's 8.6 million TEUs, Shanghai's total volume surpassed that of Pusan in both April and May and is likely to surpass Pusan as the world's third busiest port in 2003.

Ironically, there were several silver linings for China-South Korea relations related to the SARS epidemic. Increased automobile sales in China were reportedly spurred by desires to avoid public transportation and the concomitant risks of contracting SARS through close personal contact with SARS carriers; Hyundai and Kia both reported double-digit volume increases over previous month sales in China in March and April.

Although Korea had tens of thousands of students and businessmen in China during the course of the epidemic, there were relatively few returning Koreans diagnosed with the disease. One popular rumor that Koreans enjoyed citing was that *kimchi* may have medicinal properties that helped to ward off SARS. This theory gained some legitimacy from doctors who argued that allicin (also common in garlic) and lactic acid bacteria are key antibiotics that can ward off disease. Some *kimchi* skeptics argued alternatively that the low number of SARS cases said more about the low level of globalization and individual interaction outside their own community. Regardless of the reason for Koreans' relative immunity to SARS, *kimchi* joined fortunetellers and green bean soup as popular home remedies in China, driving up exports of popular *kimchi* brands such as Doosan Food BG's "Chongga Kimchi" and Dongwon F&B's "Yangban Kimchi" by 40-

50 percent in the first four months of the year. The SARS epidemic and the resultant decrease in the volume of travel between Korea and China also reduced the availability of illegal drugs in Korea; the number of reported drug cases dropped in the first five months of the year by more than 43 percent from the previous year.

SARS also played a role in China's relations with Pyongyang, as North Korea quarantined itself from the deadly effects of SARS, cutting off the twice-weekly Beijing-Pyongyang route and refusing NGO delegations from South Korea and other countries. Even for those who might consider visiting, the mandatory two-week quarantine outside Pyongyang would be enough to make many prospective visitors reconsider their plans. The extent to which North Korea's self-isolation was due to SARS or was a response to China's stern messages regarding North Korea's nuclear program remains unclear. SARS also temporarily disrupted the return of North Koreans citizens detained in China, but, by June, China was able to resume the return of over 700 detainees who were apprehended on the Chinese side of the border. China's continuous repatriations of North Koreans unlucky enough to be caught by Chinese police have been a source of tension and condemnation by human rights groups who have accused China of disregarding its own commitments under international human rights law by failing to allow the UN High Commission on Refugees to interview North Koreans to determine whether these refugees have fled North Korea for economic or political reasons.

Looking Ahead: Anticipating the First Hu-Roh Summit

After a political transition in leadership in both the PRC and South Korea, the third quarter will open with the first-ever summit meeting in Beijing between PRC President Hu Jintao and ROK President Roh Moo-hyun. Both leaders will no doubt be eager to reaffirm support for a continuously expanding bilateral economic relationship, the most recent manifestations of which include the establishment of a joint research center in strategic sectors such as computer memory chips and a steady flow of South Korean foreign investment in China-based factories to take advantage of China's low labor costs. But the geopolitical issue of how China manages its relationship and policy with the two Koreas – as well as how China positions itself in relationship to Seoul and Washington – will be the overarching strategic discussion. The matter of how to handle North Korean refugees deserves further discussion and joint action, but remains so sensitive that it is unlikely to be high on the summit agenda.

Although South Korea and China have maintained parallel policies in favor of dialogue and engagement with North Korea, neither country alone – or even together – is likely to be able to restrain either North Korea or the United States from the current path toward confrontation. Whether it is possible to peacefully resolve tensions on the Korean Peninsula – and how South Korea and China are able to limit the risks or collateral damage that could come from conflict if multilateral diplomacy fails – are key issues in the next phase of China-Korea relations.

Chronology of China-Korea Relations April-June 2003

April 3, 2003: Korean firms including Samsung, POSCO, and LG initiate steps to recall or restrict travel by employees to SARS-affected areas of China and Southeast Asia.

April 5, 2003: Korean Air and Asiana Airlines announce that they are temporarily cutting back or halting flights to areas of mainland China affected by SARS.

April 10-12, 2003: ROK Foreign Minister Yoon Young-kwan meets PRC Foreign Minister Li Zhaoxing in Beijing. Both sides agree to cooperate in establishing a multilateral dialogue including North Korea to resolve nuclear tensions on the Korean Peninsula.

April 14-15, 2003: Reports circulate that the PRC will host talks on North Korea's nuclear program in Beijing including the U.S. and North Korea April 23-25. PRC press spokesman Liu Jianchao clarifies that China is not opposed to "relevant countries" taking part in multilateral talks on North Korea's nuclear program.

April 18, 2003: PRC Ambassador to the ROK Li Bin says that the PRC does not intend to mediate between the U.S. and North Korea and that any issues regarding the Peninsula should be resolved between the two Koreas.

April 22, 2003: The Korean Sharing Movement announces that the DPRK has asked South Korean humanitarian organizations to delay visits to Pyongyang due to precautions taken as a result of SARS.

April 22, 2003: PRC President Hu Jintao meets with Deputy Chairman of the DPRK Defense Commission Gen. Cho Myong-rok.

April 23-25, 2003: PRC hosts talks with the U.S. and the DPRK on North Korea's nuclear weapons program.

April 26, 2003: ASEAN Plus Three meeting in Kuala Lumpur, Malaysia on SARS.

May 2, 2003: ROK President Roh Moo-hyun and PRC President Hu agree to continue efforts to peacefully resolve the North Korean nuclear crisis in a telephone conversation.

May 8, 2003: Samsung Electronics announces that it is delaying the opening of its second household appliances plant in Suzhou, Zhangzhou Province, due to SARS.

May 9, 2003: According to the British daily *Independent*, North Korea has quarantined 20 foreigners and closed its borders to prevent SARS from entering North Korea. Air Koryo canceled its twice weekly flight to Beijing.

May 10, 2003: PRC Vice Foreign Minister Wang Yi travels to Seoul to discuss the North Korean nuclear issue with senior South Korean officials, including South Korean counterpart Kim Jae-sup.

May 19, 2003: ROK Ministry of Commerce, Industry, and Energy announces that Korean investment in China in the first quarter increased by 120 percent year-on-year to \$310 million. Korean investment in China was 39.8 percent of Korea's total overseas investment during this period.

May 22, 2003: Two South Koreans, including *New York Times* photographer Seok Jae-hyun and human rights activist Choi Young-hoon, are among five people sentenced to prison terms of up to five years for helping a group of North Korean defectors board a ship to Korea from Yantai, China.

June 3, 2003: Korea Trade-Investment Promotion Agency announces that Korean exporters have aggressively expanded their share of exports to China from 5.16 percent to 9.68 percent during the past decade.

June 4, 2003: Tianshan Industrial Company Ltd., announces that Korean firms will participate in a construction project to build the largest high-tech industrial park in Hebei Province, a 660,000 sq. meter project to be completed by 2005 known as the Tianshan Science and Technology Industrial Park.

June 4, 2003: Korean businessmen and students start to return to China after the subsiding of the SARS epidemic.

June 11, 2003: Korea Trade-Investment Promotion Agency projects that losses to Korean investors in China due to SARS will reach \$2.5 billion by the end of June.

June 17, 2003: A study of the Korean Federation of Textile Industries projects that China's textile exports in 2005 are likely to compose 50 percent of the global textile and apparel market.

June 17-18, 2003: ROK FM Yoon and PRC FM Li discuss the North Korean nuclear issue on the sidelines of the ARF in Phnom Penh.

June 18, 2003: Korea International Trade Association announces that \$30.33 million of kimchi exports in the first four months of 2003 are on track for a record performance, outstripping prior year exports by 38.4 percent.

June 19, 2003: Samsung Electronics announces plans to set up a computer memory chip research and development center in Suzhou, China.

June 20, 2003: Ruling party President Chyung Dai-chul meets with President Hu in Beijing and urges him to hold a summit with North Korea's supreme leader Kim Jong-il to persuade North Korea to accept multilateral talks.