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NORTHEAST ASIAN ECONOMIC COOPERATION AND THE TUMEN RIVER AREA DEVELOPMENT PROJECT*

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Introduction

The Tumen River Area Development Project is a plan for a multi-billion dollar trade and transport mega-complex in the Tumen River delta. It is one of the most far reaching strategic economic ventures ever proposed for Northeast Asia and has been widely discussed both at United Nations sponsored meetings and in the public press.[1] The scope of the project epitomizes both the problems and tantalizing prospects of Northeast Asian regional cooperation and development. Embedded in the proposals are important implications for the trade and foreign affairs policies of the region and its Pacific trading partners such as Canada, the United States and Australia.

The area most immediately affected by the Tumen River Project is comprised of North Korea (DPRK), China (especially the northeast province of Jilin), and the old Soviet Far East (referred to in this paper as Pacific Russia). Other important areas that play a role in the project are China's northeast provinces of Heilongjiang, Liaoning and the Inner Mongolia Autonomous Region, and Mongolia, South Korea (ROK) and Japan.

In much of Northeast Asia strong economic growth has continued in recent years despite economic recessions elsewhere. How has it been

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[1] See references later in this paper. Also see United Nations Development Program (hereafter UNDP) (1992), "Tumen River Initiative Enters Pre-Feasibility Stage," Press Release, October 6, Beijing; C.L. Guo, "The New International Environment and Northeast Asia, *Korean Journal of International Studies*, vol. 21, no. 4 (1990), pp. 523–38; *China Daily*, 1992, various issues; 'Tumen Delta: Future Metropolis," *Far Eastern Economic Review* (hereafter *FEER*), 16 January 1992; "A Very Special Zone," *FEER*, 14 May 1992; and "Zone of Dreams," *FEER*, 28 May 1992.

sustained? The Pacific Economic Cooperation Council (PECC) has become an important regional forum for dialogue on commercial and economic issues. As recently as September 1992, the council committed its members to "open regionalism" and increased economic integration.[2] Trade, capital flows and some labour movements among the Northeast Asian countries have continued to increase. The trend towards globalization of Japanese production continued.[3] South Korean firms' production is currently concentrated in Asia but they too are rapidly following the Japanese expansion model.

Northeast Asia also faces political uncertainties in the 1990s. In spite of the emergence of a more benign international setting, there remains the potential for instability. Leadership succession crises loom in the DPRK and in China. There is a continuing buildup of tension in China between liberal economic reform and the ideological rigidity of an autarkic political system. The process of *rapprochement* on the Korean Peninsula, popular tests of the ROK's new political arrangements, and stagnation of political and electoral reform in Japan are issues to be followed with close attention.

While economic growth has created pressures for political liberalization, divergent trends have also emerged because of political and institutional arrangements peculiar to the various parts of the region. Where the process of democratization has advanced, such as in the ROK, and even in Mongolia and Pacific Russia, more diverse interest groups have enhanced their capacity to influence national policies. A trend towards greater preoccupation with regional affairs on the part of Japan and China, detectable in their recent foreign policy emphases, is likely to continue. Growing economic strength in the more advanced economies of Northeast Asia, and a lowering of some political barriers previously imposed by the cold war atmosphere are helping to foster a regional orientation and enhanced political self-confidence. The weaker economies of the area (Mongolia, Pacific Russia, DPRK, and to a lesser extent China) more cautiously view

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[2] Asia Pacific Foundation of Canada, "PECC's San Francisco Declaration Commits 20 Pacific Rim Countries to Open Regionalism," *Dialogue*, vol. 6, no. 4 (1992), p. 8.

[3] By globalization we mean the expansion of firms with fully integrated plants in several countries and the international flow of capital and other resources to support these, often a resource or factor flow within the firm. R. Aliyer, "Emerging Economic Role in Northeast Asia and Response of the Soviet Union: Economic and Political Aspects," *Korean Journal of International Studies*, vol. 23, no. 1 (1992), pp. 1–14; G. Boyd, "Japan in the Pacific Policy Environment for Strategic Planning," in P.N. Nemetz, ed., *The Pacific Rim: Investment, Development and Trade* (Vancouver: UBC Press, 1990), pp. 195–210.

Table 1. Population of Northeast Asia Region, 1989

	Area 000s km.	Population 000s	Density Pop./km.^{2}
Soviet Far East (Pacific Russia)*	6,216	71,941	1.3
Northeast China	787	97,890	124.3
Inner Mongolia	1,183	21,220	17.9
North Korea	125	21,370	170.6
South Korea (1990)	99	43,550	439.5
Japan (1988)	378	122,783	329.3
Total	8,788	314,724	35.8

* Includes Kamchatka, Magadan, Amur, Sakhalin, Maritime and Khabarovsk.

regional orientation as a means of attempting to deal with their own economic malaise.

The next section of this paper summarizes the major trends in regional growth and development and highlights features of the region and its countries that influence intraregional integration. Section 3 places Northeast Asian economic growth in its international context. The main part of this study—sections 4 to 6—reviews the state of the Tumen River Development Program and its role in promoting Northeast Asian economic cooperation, and provides an analysis of the complex political economy of the proposals. The concluding section examines the regional and international implications of the Tumen project.

Trends in Regional Growth and Development

Northeast Asia has been one of the fastest growing regions of the world over the past decade, with annual real GNP growth averaging over 7 percent during the 1980s. By 1989 the region had reached a population of almost 315 million unevenly divided between the main components of the region—see table 1. Approximately 50 percent of the population resided in the two developed countries of South Korea and Japan which account for proportionately more of the regional GDP. The other regional economies which accounted for a smaller proportion of the regional GDP had less developed industrial structures with much higher proportions of their economies in the traditional sectors, particularly agriculture. Some of these smaller economies have, however, relatively abundant natural resources. This provides the base for increased trade both within the region, as in the case of South Korea and China, and with the outside. Not surprisingly, the economies which exhibit the higher GDP growth are those whose trade sectors are growing most rapidly.[4]

One factor necessary for continued economic growth in Northeast Asia will be the ability to move resources rapidly to different sectors in order to effect structural change. Earlier structural change involved basic movement out of agriculture into manufacturing and then through various levels of capital-intensive production. More recent development, often involving changes in methods and technologies rather than major shifts in the focus of industry, has produced a sophisticated pattern of specialization based on an even more pronounced regional division of labor.

One of the background arguments supporting the development of a trade and transport complex (in the form of an economic zone) in the region is the unprecedented trade liberalization of recent years especially in the case of Japan and the ROK. China's continued reform of its foreign trade system, though patchy and often imposed as a last minute reaction to external pressures, has strengthened the trend towards greater openness and integration into the regional economy. The changing regional pattern of growth and structural change has been accompanied by new patterns of trade flows, including bigger shares of world exports and imports and marked growth in intra-industry trade because of increasingly open manufacturing sectors. Apart from greater trade in finished products such as automobiles and consumer electronics, for example, trade in intermediate products within particular industries is increasing, attesting to the trend in the globalization of production.

Economic integration of the Northeast Asian economies is likely to continue to deepen. This, in turn, will continue to lead to increased interest in the development of what have been referred to as "sub-regional concept zones" such as the Japan Sea Rim (Japan, China, the Korean Peninsula and Pacific Russia), the Yellow Sea Economic Cooperation Zone (China, the Korean Peninsula and part of Japan), the Bohai Economic Zone (Northeast China and the Korean Peninsula), or specific cross boundary proposals such as the Tumen River Project (China, DPRK, Pacific Russia, and

[4] S. Atkinson, "The USSR and the Pacific Century," *Asian Survey*, vol. 30 (1990), pp. 629–45; *FEER*, "Russian Far East and Siberia," in *Asia 1994 Yearbook* (Hong Kong: Review Publishing, 1994), pp. 196–99; K.E. Calder, "The North Pacific Triangle: Sources of Economic and Political Transformation," *Journal of Northeast Asian Studies*, vol. 8 (1989), pp. 3–17; Y.K. Cha, "The Changing International Order and Northeast Asia in the 21st Century," *Korea and World Affairs*, vol. 15, no. 4 (1991), pp. 640–50; and Q.D. Chen, "Newly Emerging Economic Order in Northeast Asia," *Korean Journal of International Studies*, vol. 22, no. 4 (1991), pp. 593–605.

the ROK).[5] Post-cold war geopolitical restructuring and the pace of rapprochement between capitalist, socialist, and formerly socialist countries of the region will affect the evolution of such developments. If present trends continue, it appears likely that the DPRK, Pacific Russia, and perhaps even Mongolia, will be drawn into the growth orbit of Northeast Asia through involvement in such subregional developments.

The regional trade pattern shows every indication that it will be characterized by: diversity, increased technological competition, and higher levels of intraregional and intra-industry trade.[6] Although rates of growth of national income will be high by global standards, they will probably be more moderate than those experienced by the region during the 1980s. Over the next five years Northeast Asian economic policy makers will face the additional challenge of managing inflationary pressures while the process of structural change continues at a rapid pace. A key element of this process will be managing competing political goals as economies are opened still more to international trade influences.

The rapid growth in real GNP has, of course, not been evenly experienced. This is particularly evident in China where regional (i.e., subnational) income per capita now differs substantially. Shenzhen residents experience an annual income that is two and a half times that of citizens of Beijing—but because of differences in local prices this may overstate the standard-of-living difference.[7] Regional disparities in real per capita income often emerge, or are amplified, during periods of rapid economic growth; this is particularly so in so-called developing economies.[8] However, modern economic growth in the economies of North America and Western Europe has been accompanied by declining regional inequality as the structure of the regions takes on more of the characteristics of the whole and as policies of regional redistribution are initiated. The Tumen River Project will likely have important redistributive aspects.

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[5] *FEER* (1993), *Asia 1993 Yearbook*, pp. 64–65.

[6] A. Hansson and J.H. Helliwell, "The Evolution of Income and Competitiveness in the North Pacific Rim," in F. Langdon, ed., *Canada and the Growing Presence of Asia* (Institute of Asian Research, University of British Columbia, 1990), pp. 17–40.

[7] State Statistical Bureau, *Statistical Yearbook of China 1990*, People's Republic of China, Beijing.

[8] The Kuznets Curve measures per capita income growth and personal income inequality. See P. Lindert and J. Williamson, "Growth, Equality and History," *Explorations in Economic History*, vol. 22, no. 4 (1985), pp. 341–77.

The essential policy agenda for Northeast Asia remains unchanged. As Elek has recently pointed out, these are[9] (1) improving market access; (2) reducing uncertainty in output and product markets; (3) reducing physical bottlenecks; and (4) harmonization of domestic legislation and rules of market behavior.

The minimum condition for the Tumen River Project to be successful is that there be a heightened pace of nondiscriminatory trade liberalization, more effective exchanges of information, and a harmonization of the customs practices, including documentation.

International Economic Environment

As the region has become more deeply integrated with the international economy its engagement with other parts of the world is becoming more complex. This is reflected in, among other things, a substantially increasing share of world output and trade, the spread of production and technology, developments in transportation and communications which have intimately linked the economies to major international centres, and diversification of export markets.

With its increasingly open, export-oriented economies, changes in the international economic environment and external market conditions have traditionally been a key factor in determining the pace and direction of economic and trade development in the region. More recently, the greater role for domestic demand, particularly in Japan and the ROK, partly driven by an international economic environment less favorable to exports, has, in turn, produced economies much less dependent on external economic conditions. Over the past two years, in addition to slower growth in major markets, international events—such as the official end of barter trade between the DPRK and China—may have temporarily reduced trade levels.[10]

The end of the cold war implies changes in defence spending. All the countries of the region face a different complex of security issues than was the case in the late 1980s. For the region as a whole, change in the former

[9] Andrew Elek, "Pacific Economic Cooperation: Policy Choices," *Asian Pacific Economic Literature*, vol. 6, no. 1 (Spring 1992), pp. 5–25.

[10] The official end of barter trade has not, however, brought unofficial barter trade to an end but the extent to which this occurs is not currently known. For a discussion see R. Garnault, "Exchange Rate Regimes in the Asian-Pacific Region," *Asian Pacific Economic Literature*, vol. 5, no. 1 (March 1991), pp. 5–25.

Soviet Union could result economically in the much touted peace dividend. For example, the prospects in the medium term of resolution of the Kurile Islands dispute between Japan and Russia are improved and could result in a large injection of capital into the region. While substantial risks lie ahead as parts of the former Soviet Union try to put in place stable institutions and negotiate workable arrangements among themselves, if the transition can be managed, Pacific Russia should begin to play a larger economic role in the region. This expected development must not be overlooked in the discussions that have been undertaken to establish new subregional areas of cooperation.[11]

Increased environmental concerns globally are reflected in the region. Northeast Asia, since it contains developed, maturing, and developing economies, to some extent represents a microcosm of the key international issues. Along with a diversity of overwhelming environmental problems, there are also challenges of integrating these concerns with the imperatives of economic growth to produce "sustainable development"; concerns that environmental policies may adversely affect trade competitiveness or that trade policies may damage the environment; concerns over the responsibilities of the developed countries and their potential role in assisting less financially and technologically capable economies; and interest in global and regional mechanisms for environmental cooperation. In particular, Japan and China are playing larger roles in leading discussion of these issues both regionally (including the Asia Pacific Economic Commission [APEC], the Economic and Social Commission for Asia and the Pacific [ESCAP], the Asian Development Bank [ADB], and the Pacific Economic Cooperation Council [PECC]) and internationally (in the UN, OECD, and the World Bank). This is just one aspect of the increasing role both countries are seeking in regional and global affairs.

Since the mid-1980s there has been a growing interest in the ramifications of regional developments which include a single European market, moves towards a European Economic Area including the European Free Trade Agreement countries, and the development of the North American Free Trade Agreement. There has also been a spate of proposals focusing on the Asian region which have emerged partly as a result of the other moves towards regional arrangements and fears of being left out, and

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[11] Following discussions at the Vancouver Summit in April 1993 and a meeting of the G7 finance ministers in Tokyo, also in April 1993, a multi-billion dollar aid package was announced to support economic (and political) reforms in Russia.

partly as a recognition of the growth in intraregional trade and integration between economics of the region. PECC, for example, has become the major economic forum in the Asia Pacific region. PECC may have an increasingly important role in managing economic and trade differences, for instance between Japan and the United States. In the event of diminishing results from multilateral efforts, the focus of trade policy may, in fact, become sectoral or industry-based rather than regional or bilateral. These efforts need not be mutually exclusive. APEC is also well placed to provide a focus for sectoral and regional initiatives while keeping them consistent with multilateral principles. Regional economic cooperation will remain high on the agenda for the countries of Northeast Asia particularly with the successful conclusion of the Uruguay Round.

The Tumen River Development Project

The United Nations Development Program (UNDP) has taken the lead in promoting the Tumen River Project and the rapidity with which the proposal has been advanced has, to date, outstripped the policy response. Straddling the border region between the DPRK, Pacific Russia, and China's Jilin Province (see figure 1) the proposal must confront directly a number of the challenges outlined in the preceding section of this paper. Because of the complex diplomacy required to map strategies for its development the Tumen project will challenge the drive for greater economic cooperation in the region.[12] In addition to the three countries most directly involved, and across whose territory the project will be located, the ROK and Japan are seen as potential beneficiaries and sources of the enormous financing that will be required. Land-locked Mongolia's interest lies with the possibility of gaining another less congested link with the Pacific.

The first plan ("Option A") is the development of three so-called growth centres—in the undeveloped ports of Rajin in the DPRK, Posyet in Pacific Russia, and an island transshipment zone around Hunchun in China. With a view to integrating them later China has already designated Hunchun as another "open" city indicating central government support for development in the region while the DPRK has promised similar status to the

[12] S. Harris and J. Cotton, eds., *The End of the Cold War in Northeast Asia* (Melbourne: Longman, 1991); and R. Garnault, *Australia and the Northeast Asian Ascendancy* (Canberra: Australian Government Publishing Service, 1989); C.S. Kim, "Economic Cooperation in Northeast Asia," *Korean Journal of International Studies*, vol. 22, no. 1 (1991), pp. 55–74.

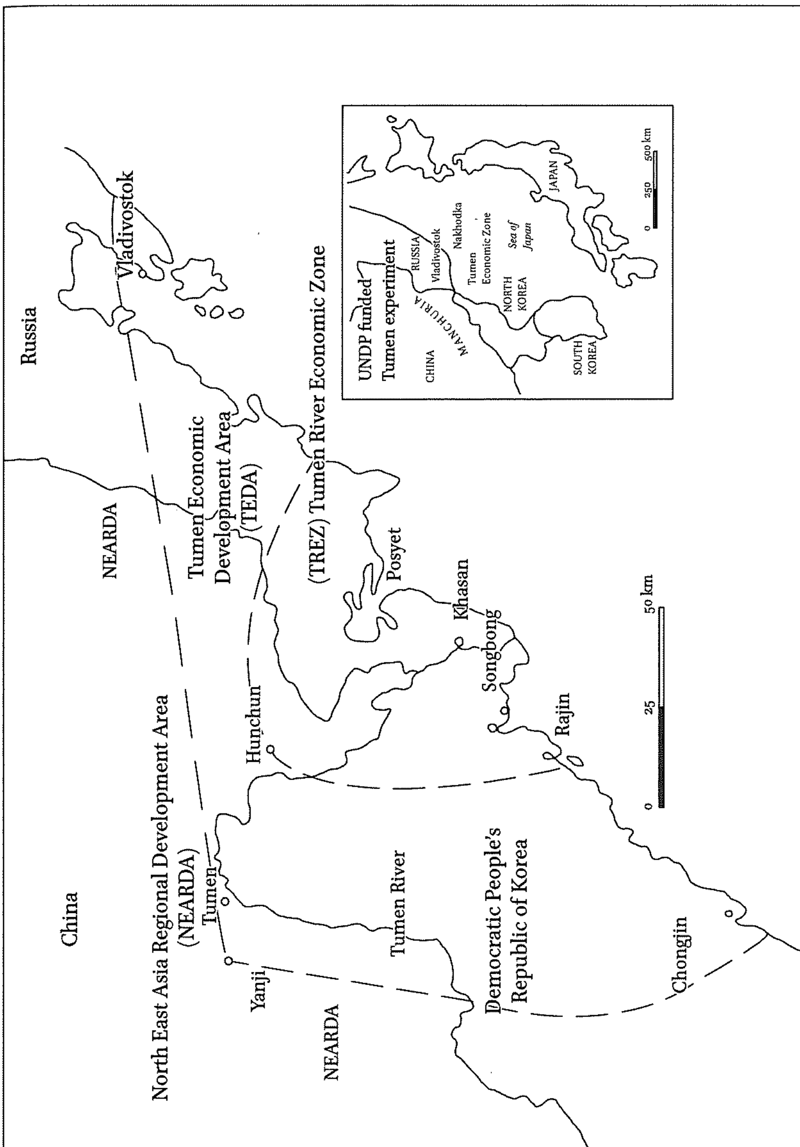

Figure 1. Tumen River Delta Area with Large/Small Development Zones.

corresponding area of Songbong and Rajin within its territory. A loose association of three (free) economic zones would be coordinated through a Commission for Cooperative Development which would deal with common concerns about port, railroad, and other infrastructure development. The DPRK is the most avid proponent of this option since they are unwilling to cede any of their territory to an internationally managed zone. Under the Option A arrangement the zones would compete for investment to promote development.

Some advantages of Option A are that (1) it could be relatively quickly implemented; (2) concerns over sovereignty would be allayed; and (3) each riparian state would control the development in its respective zone. Disadvantages include the difficulty of marketing a disparate and loosely coordinated number of zones lacking a set of unified rules to attract investors. Lack of coordination would also slow the pace of the project. Each country would also face "sovereign risks" as investors seek government guarantees. Further, representations from the non-riparian state of Mongolia have consistently indicated their desire to negotiate with only one international body in the Tumen River Area Development Program (TRADP). Currently, Option A is considered as the consensus proposal on which to base a management plan.

"Option B" is a more integrated proposal calling for multilateral development of the entire Tumen region with an international decision-making authority. Each of the riparian states would lease approximately three hundred square kilometres of land to the TRADP which, in turn, would establish a Commission for Cooperative Development as in Option A, but also create a system of shareholding in a Tumen River area management company. This "solution" as it has evolved typifies the agglomerate approach that most regional development advocates favor and would involve not just the riparian states, but also Mongolia, South Korea, Japan, and agencies such as the Asian Development Bank and the World Bank. Features of this option include a single unified free economic zone managed through one negotiated master plan (by treaty) for the cooperation, operation, promotion, and development of the region. Aspects of existing international regional management schemes such as the Danube River Commission, the St. Lawrence Seaway Authority, and the Johore-Singapore-Riau growth triangle could provide the basis for a locally developed model for the Tumen project.

Unified control could more easily attract international investment, lead to a faster pace of development, and contribute to enhanced economic stability in the region. However, this arrangement would involve a long period of complex negotiation which in the end some participants may choose not to accept. International management is successful only when all contracting states acquiesce and agree to sublimate national political issues. Unfortunately, there is no tradition of cooperation in the region which would suggest effective management based on this type of behavior.

A third plan has emerged, "Option C", which attempts to resolve some of the apparent problems of the other schemes. This proposal has been called an "oil spot" development for a Tumen River Economic Zone (TREZ) in which a twelve-square-kilometre United Nations core city[13] is linked by a series of development corridors to free economic zones in satellite cities in the regions of Hunchun, Rajin/Songbong, and Posyet/Khasan (see map on page 1). Land for the core city and development corridors would be leased to an international management commission in which national sovereignty would be limited to social issues only. Negotiations for development contracts, taxes, and similar economic matters within this area would occur under the authority of a corporate entity while the individual competitive free economic zones would be directly administered by the respective governments.

The Democratic People's Republic of Korea has been the most reluctant of the three riparian states to relinquish any national sovereignty. However, there are some indications that the DPRK is on the verge of accepting this proposal. In September 1992 DPRK officials invited their Chinese counterparts to "explain" the advantages of Chinese-style special economic zones and how they dealt with issues of foreign ownership and investment. In the context of the political sensitivities of Northeast Asia this is a significant positive development.

A fourth option, only partially explored in the official discourse, is much less coherent than the other schemes proposed. It is loosely based on an amalgam of the other options. Although Option A stresses government control of TRADP, and the other options various levels of private sector control, the two types of strategy share some common ground. Even if participant countries individually implement their own competitive free economic zones (linked or otherwise) they must still agree to regional trade and transit improvements in order to facilitate their growth and prosperity. Without such agreement, individual plans for the Tumen River are not feasible, especially in the case of China and the DPRK. Moreover,

[13] To be called the "District of Harmony and Prosperity."

this approach might accommodate greater regional variation in the pace of development based on different levels of commitment and investment. Under this proposal the original "Rotterdam of the East" vision of TRADP might be shown to be not only unworkable, but perhaps unnecessary.

Prospects for the Tumen Project and Northeast Asian Economic Cooperation

(a) *Economic Rationale for TRADP*

For the Tumen River Area Development Program to be successful under one or any combination of the options explored above it must have a clear economic justification. First must be an immediate potential for trade enhancement as a result of a growing willingness to remove political, tariff, and physical barriers among participating countries—trade creation and trade diversion. To tap this potential, TRADP would have to implement specific proposals concerning the reduction of tariff and non-tariff trade barriers; the standardization of trade documents; the collection and dissemination of trade statistics and related data base development; and the identification of physical barriers to trade, and form a plan for infrastructure and institutional improvements. It is unlikely that the prospects for increased trade *among* the states of a Northeast Asia Regional Development Area (NEARDA) by themselves could justify an economic zone at the mouth of the Tumen River. Mongolia, China, Russia, and the DPRK have between them long borders that already experience substantial trade and transit. As with existing trade, any new trade between Mongolia and China, China and Russia, or Mongolia and Russia has more direct routes than through the Tumen River area. The only exceptions are border trade originating in the immediate vicinity of the Tumen River.

Second, transport cost efficiencies—the welfare gains from trade—may result from new shipping and rail links associated with the new facilities in the Tumen River area. Against the cost of the Tumen River transport facilities must be measured the cost of improving the existing ports of Vladivostok, Rajin or Chongjin. It is not self-evident which alternative would lead to the greatest economic benefits in the region.

Third, there is a potential that results from economic complementarities in the Tumen River Economic Zone and its hinterland. The states are very differently endowed with resources and levels of savings. Infrastructure and land resources are immobile and cannot be traded. The development of a small but nonetheless significant transnational labour market in recent years is an indication of the potential. China's local water and energy resources could be put to area use.

Although there is a significant potential for increasing trade among the partners, quantification of this potential is difficult. Furthermore, while China has undertaken more than a decade of reforms the DPRK continues to pursue a policy of "juchai" (self-reliance) and Russia and Mongolia have only just initiated significant restructuring of their economies. In this political climate changes are likely to occur slowly and absorb large amounts of human and financial resources.

A set of measures that facilitate trade may be more beneficial than an overarching scheme. In Russia this means improving the management and utilization of the existing infrastructure, including the port capacities in Vladivostok and Nakhodka. For Chinese, Russian and DPRK cooperation, it requires improved transit facilities at the borders, including minor investments in facilities for railway gauge changes, composite rail, and other measures that increase existing rail transport capacity. Meanwhile, idle capacity has developed in many parts of Russia's economy such as in the naval shipyards and military industrial sector of a post-cold war Vladivostok.

It should be noted that the participating countries emphasize different aspects of the Tumen River project. Some see the benefit of the immediate effect whereas others focus on the longer run consequences. China, for example, while acknowledging the importance of short-term trade development, has indicated that TRADP should pay most attention to the longer run goals by providing for change in the legal structure, the social overhead capital, communications, and financial/investment in order to implement the Tumen River Economic Zone. Other participants, such as the Primorski District of Russia, are of the view that TRADP should highlight development of intra-subregional trade within the overall framework of the larger geographic area (i.e., one which includes the Greater Vladivostok Economic Zone).

The scale and scope of the program should be flexible. As Northeast Asian economies undergo fundamental changes, their course is difficult to predict. Trading patterns remain erratic, and the continued use of administered prices makes it difficult to estimate future gains from trade, or the volume and pattern of trade. Under these circumstances it is likely more advantageous to let infrastructure development follow rather than lead demand. In other words participant countries and international investors should expect greater than usual risks from a strategy of large front-end investments. In practical terms, this advises caution in developing an international airport and large container port as part of an immediate first stage development program as is currently being contemplated. Capital limitations of participant countries and the "restructuring" and shifting priorities of international funding agencies may preclude the high initial investments in any case.

Any international treaty among participant countries should not only deal with TREZ, but should also give equal importance to trade, transit, and transport facilitation in the broader NEARDA region. Trade facilitation is not specifically a TREZ issue, it deals only marginally with physical planning, and it applies to the region at large, rather than just to any specific border site. There is probably no better way to convince investors about the potential of TREZ than to demonstrate that existing port and transport facilities are fully utilized, that border trade is booming, and that participant countries have eliminated traditional barriers to border transit and fully cooperate in the joint use of their transport networks. It would be difficult to convince any investor to build new facilities in the immediate vicinity of existing ports in the DPRK or Russia that have excess capacity. Hence, the enhancement of trade and the improved management of existing infrastructure resources should be seen as essential steps for the first phase of TREZ.

(b) *Trade Enhancement among Participating Countries*

Although border trade has been growing over the past few years it continues to be small. Border trade in China's Jilin Province is estimated at 10 percent of its total foreign trade in spite of its common borders with Russia and the DPRK. In Primorski, the share of border trade including coastal trade has stagnated since 1988 at about 30 percent.[14] Highly centralized bureaucracies that manage trade have different interests from those of border areas and often lack adequate local knowledge. Authorizing more enterprises to trade, decentralizing export licensing systems, and encouraging third party transactions would enhance border trade, thereby promoting the intensity of bilateral relations among the riparian territories. Evidence of increased trade and other exchanges by individuals (such as

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[14] UNDP, "Subregional Trade Expansion in Northeast Asia in the Context of the Tumen River Area Development Programme" (1992), and various reports and other documentation of the *Program Management Committee: Second Meeting* held in Beijing, October 9–11, 1992. Also, UNDP, *Program Management Committee III: Reference Matrices Covering Institutional, Legal and Financial Issues* (Pyongyang, 1993).

in education) should also be highlighted as an important aspect of the border economy.[15] This activity can provide large numbers of people who are able to assess the conditions of supply and demand and the resulting business opportunities. Individual trade also exposes enterprises to competition, forcing them to concentrate on areas in which they have comparative advantage. Moreover, this type of trade would encourage the diffusion of production technology and marketing know-how within the Tumen River delta.

But the ultimate success of TRADP depends largely upon the credibility of the program within the enterprise sector. Will financial institutions be ready to fund infrastructure upgrading? Will foreign trade companies take the initiative of intensifying exchange among the riparian territories? Will transport and other trade support companies develop their services along TRADP's transport corridors? Will investors from the subregion and third countries be willing to invest in the Tumen River delta? Currently, the Tumen project can be considered in business circles only as a promising, but high risk investment. Yet participation of the enterprise sector in TRADP can still be promoted. Indeed, information and promotional events have already been organized, such as recent appeals for investment in the Rajin-Songbong Free Trade Zone—the DPRK's contribution to TRADP.[16] In addition a business advisory committee to the TRADP could serve as an umbrella for private initiatives and business groups taking a particular interest in the Tumen River delta and the riparian territories in general.

Barter deals are still the most common form of trade among the riparian countries with the principal advantage that they do not require the use of convertible exchange. On the other hand, transaction costs are high since it is difficult to find a partner who is interested in both sides of the deal, and transactions are often crude as it is difficult to correctly set prices and quantity. An important bottleneck factor for expanding trade with China is the lack of suitable goods on local markets in Primorski and the DPRK. Moreover, product specifications for barter deals do not always seem to be sufficiently clear. As a result of these problems barter trade is simple to conclude, but difficult to transact with implementation of barter contracts between riparian territories at or well below 25 percent

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[15] J.C. Baek, "North Korea's Relationship with the Soviet Union and China: Implications for Peace on the Korean Peninsula," *Korean Journal of International Studies*, vol. 22, no. 2 (1991), pp. 181–95; L. Kaye, "Creative Tensions," *FEER*, 7 January 1993, pp. 16–17; and J. Lilley, "Travellers' Tales," *FEER*, 11 February 1993, p. 30.

[16] M. Clifford, "Send Money," *FEER*, 30 September 1993, p. 72.

of contract volume.[17] In this context it may be useful to organize legal workshops with experts from participating countries to improve barter contracts focusing especially on arbitration clauses, delivery terms and product specifications. Such expertise could come from South Korean conglomerates, general trading companies from Japan, or firms specializing in compensation trade with central and eastern Europe.

Trade expansion in the subregion would be facilitated by an upgrading of trade support services in the participating countries. This requires closer collaboration and networking among trade support institutions and, in particular, among foreign trade research institutes and departments of statistics in charge of collecting and presenting trade and industrial data. Considerable expertise in these areas is available in some countries of the subregion (i.e., Japan, ROK, China), which can be harnessed for improving the level in all participating countries. Networking among similar trade support institutions in the subregion should advance in parallel with networking in the enterprise sector. Participating countries, particularly Mongolia, Pacific Russia and the DPRK, should give priority to national trade facilitation programs. As part of this process trade documentation needs to be aligned to international standards to make transactions less expensive and less complicated.

Direct investment in the Tumen River area and among participating countries should be seen as a powerful tool for promoting economic cooperation. This is particularly so if goods can cross borders less easily than capital or labour due to barriers such as high tariffs and quotas, transport problems, and difficulties in currency exchange. Although there is a growing number of investments among the three riparian countries the order of magnitude of the investments remains small and many joint ventures have gone into nonproducing service sectors such as restaurants and hotels.[18] Furthermore, investment from third countries is more likely to accelerate once the major infrastructure problems have been solved and market access for producing firms in the Tumen River area to all riparian countries has been negotiated. Thus government authorities at all levels should endeavor to identify and remove barriers to direct investment with a view to strengthening economic relations. Primary and manufacturing sector investment as well as in trade-related services such as transport

[17] UNDP (1992), p. 15.
[18] See Kaye, "Creative Tensions."

and finance should be actively encouraged, particularly through the creation of joint ventures.

Perhaps the most important component of trade enhancement, and the one element which underlies all the others, is the establishment of a data base on industry and trade. Basic information on trade and economic relations among the five participating countries must be improved to provide a basis for planning and infrastructural development within TRADP, and for presenting and promoting the Tumen River area, and Northeast Asia in general, to outside traders and investors. The present availability of trade data is very limited and the data that are available are often contradictory.[19] Only for the ROK and China are quality data by region and commodity currently available.

(c) *TRADP and the Importance of Trade Enhancement*

The development of trade along the lines discussed in the preceding section should be seen as the necessary driving force for the successful implementation of TRADP. The trade component is important for the success of the program in at least four aspects.

First, the development of intra-subregional and third-country trade among the participating countries generates the demand for improvements in the physical, policy and regulatory infrastructure linking the three riparian countries. A growing volume of trade through and within the Tumen River area could also provide some of the necessary financing for these improvements.

Second, the three riparian territories (Hangjong Pukto Province in the DPRK, China's Jilin Province, and Primorski District in Pacific Russia) are all undertaking considerable efforts to strengthen international trade, both intra- and extra-subregionally. This is most clearly demonstrated in the priority attached to the development of free trade zones and the rapidity with which they were implemented in each of the three riparian territories.[20] Clearly, trade development is a point of common interest. It is essential, therefore, that projected infrastructural development in the broad sense be determined and driven by the existing and future demand for improved trade and trade support services.

19 UNDP (1992), p. 16.

20 See "Five Nations to Jointly Develop Tumen Triangle," *China Daily*, 16 May 1993; Clifford, "Send Money," p. 72; *FEER*, "Russian Far East and Siberia," in Asia 1994 Yearbook, Hong Kong: Review Publishing, pp. 196–199.

Third, the development of trade will strengthen the fabric of economic relations among the three riparian countries. Not only does it create the volume of exchanges required to finance major infrastructural improvements, it also helps to create more stable economic relations because it multiplies the number of enterprises and institutions with a vested interest in further improving subregional economic relations. This will serve to strengthen the basis for the more ambitious components of TRADP.

Fourth, promotion of trade activities among the participating countries will yield direct and tangible results with limited risk. In other words, since present trade clearly remains below its potential, and the interest of enterprises and trade support institutions in the participating countries in trade expansion is pronounced, all concerned have little to lose and much to gain.

Negotiating the conditions for increased trade is, however, complex and their implementation full of political and economic hazard. In the following section we look at the political economy of these issues in the Tumen project context.

The Political Economy of the Tumen Project

(a) *Processes of Regional Economic Integration*

Preliminary discussion and commentary regarding the Tumen Project seem to reveal at least three not entirely distinct views.

First, those who are most avid supporters of the project, especially China and the DPRK, are anxious to press ahead with the program of development in spite of the enormous obstacles—geopolitical, financial or jurisdictional. They argue that it is important to take full advantage of what they perceive as a "window of opportunity" to undertake cooperative development. The dramatic changes of the past two years have eased tensions to a point where, at the very least, all six of the political entities concerned can sit at the same table. Presently, the border region is relatively undeveloped, leading to the view that there is an opportunity to "do it right" by planning a comprehensive project from the outset. The involvement of all those concerned from the earliest stages of development, the argument goes, is more likely to ensure a commitment to overcome the difficult issues which will inevitably arise and to promote the ultimate success of the project.

The second general response expresses deep concerns about the inability of such a complex and essentially unknown entity to function well.

Although there does not appear to be any outright opposition to the project proposals, other countries, especially Japan and the ROK, have been particularly cautious in their initial response to the proposals. As might be expected those who are expected to fund the project, primarily the ROK, Japan, the Tokyo-dominated ADB, and South Korean and Japanese industrialists, are particularly concerned.[21] Issues such as a binding legal framework, promised political stability, and dispute settlement mechanisms must be in place before there is a commitment to the massive funding required. However, a mitigating fear of being left out could mean that western construction, telecommunications, and shipping interests would be more amenable to providing, or supporting access to, the necessary funding.

A third general view questions the efficacy of the project, given the potential for conflict with existing facilities along the Sea of Japan, the Bohai Gulf, and the Yellow Sea. Critics of the Tumen Project promote the alternative of building up the infrastructure of existing ports as a means of encouraging Northeast Asian regional economic cooperation. Enhancement and rationalization of existing facilities would provide a more stable and potentially more profitable investment environment. They point to the somewhat fantastic objectives, such as establishing a "land bridge" to Europe, as unrealistic components of a very expensive project.

Since the initial UNDP-sponsored discussions in 1991 an international Program Management Committee (PMC) has been struck to establish the terms of reference for the Tumen River Area Development Program (TRADP). The PMC now includes China, Russia, North and South Korea, and Mongolia as full members and representatives from the Asian Development Bank (ADB), World Bank, and the Japanese government with observer status. The original aim of the TRADP was to assist the five participating countries jointly to formulate a long-term comprehensive plan for economic cooperation principally in the areas of industrial and trade development.

The technical support to be provided by the UNDP was initially seen as contributions to the feasibility analysis and pre-investment phases of longer-term strategies for subregional economic collaboration (that is,

[21] See "Tumen River Initiative", *SUPAR Report*, no. 11 (July 1991); "Japan Governors' Conference on Sea of Japan," *SUPAR Report*, no. 12 (January 1992), p. 28; "Jilin, Primorskii Krai Sign Agreements," *SUPAR Report*, no. 11 (July 1991), p. 30; "Osaka Mission to Study Tumen Project," *SUPAR Report*, no. 12 (July 1992), p. 37; Kaye, "Creative Tensions"; Lilley, "Travellers' Tales"; and *Asian Wall Street Journal*, various issues.

strategies in the area of industrial and trade policy, land use, transportation and physical infrastructure expansion). UNDP support was also seen as shorter-term confidence-building by giving the project the appearance of less risk than otherwise in the hope of stimulating some foreign investment (in the form of joint ventures). Any momentum gathered would aid the longer-term economic initiatives. During the inaugural PMC meeting in Seoul, in February 1992, it was generally agreed by the participants that the TRADP should initially focus on the economic and technical feasibility of, and related financing strategies for, one specific approach to intrasubregional economic collaboration. The "ultimate vision" was the creation of a multinational industrial and trade servicing zone in Northeast Asia—a "Rotterdam of the East."[22]

This so-called vision would involve some sort of amalgamation, under a coordinated management structure, of territory from the three riparian states of China, Russia, and North Korea into a contiguous export-oriented zone (referred to as the Tumen River Economic Zone or TREZ). This could include China's Hunchun, Songbon and Rajin in North Korea, and Posyet in Russia. Within this "small delta" area of TREZ, intensive development of a light industrial, financial, and trade servicing centre is envisaged. However, major issues such as international cooperation and management, and national sovereignty must be resolved before TREZ can be meaningfully implemented. Furthermore, through its backward linkages to the hinterland, TREZ would accelerate economic development of what the UNDP refers to as the Northeast Asia Regional Development Area (NEARDA). NEARDA is defined as encompassing the Chinese provinces of Heilongjiang and Jilin and the semiautonomous region of Inner Mongolia, all administrative districts of Pacific Russia, especially Primorski and Khaberovsk, all of Mongolia, the DPRK, and the ROK.

The economic sphere influenced by the TREZ would most likely be in the extraction of raw materials, and the transport and other service industry resources required to market them.[23] Coinciding with the TRADP initiative, bilateral cooperation between China's Jilin Province and Pacific

[22] The discussion here is based on the UNDP reports and documentation from the second PMC meeting held in Beijing in October 1992.

[23] S.H. Kim, (1990), "The Proposal for Forming a North Asian Economic Zone and South Korea's Position," *East Asia Review*, vol. 2, no. 4, pp. 3–14; T. Watanabe, 'Japan Sea Basin Needs Economic Cooperation; Soviet Far East Should be Central to New Zone," *Japan Economic Journal*, March 30, 1991, p. 8; and G.J.R. Linge, "Developments in Russia's Far East and Their Implications for the Pacific Basin," *Australian Geographical Studies*, vol. 30, no. 2, (1992) p. 136.

Russia's Primorski District in the Tumen River area has gained momentum. Numerous agreements have been implemented for the construction of highway, railway, telephone, and border facilities, along with trade contracts and joint projects in manufacturing and services (mostly Chinese restaurants).[24]

Integration of the TREZ and NEARDA would occur with the creation of an intermediate region identified at the conclusion of the first PMC meeting as the Tumen Economic Development Area (TEDA) (see map). TEDA might include regions and ports such as Vladivostok, Chongjin in the DPRK, and the Yambian Korean Autonomous Prefecture in China's Jilin Province. Thus, a rationalized series of modern, specialized ports would position TREZ as the principal transportation and transit entrepot for Northeast Asia and the gateway to a so-called land bridge serving the Far East trade with Central Asia and Europe.[25]

(b) *Stakeholders, Institutional Structures and Regions*

The evolving market of the region, especially between Northeast China and Pacific Russia, has been an effective driving force of regional economic integration in the area of the Tumen River. The Program Management Committee explicitly recognizes the importance of building an institutional structure which will further encourage these local developments and that will attract international private sector generated trade and investment. All of the recent UNDP-sponsored discussions regarding technical feasibility, trade enhancement, financing and project promotion hinge upon resolving the nature of the articulation between private (international) investors, local and national government stakeholders, the geographic regions to which they correspond (TREZ, TEDA, NEARDA respectively), and the institutional structures through which they will exercise their respective interests.

These issues came to a head at the third Program Management Committee meeting (PMC III) held in Pyongyang in May 1993. The delegates negotiated two agreements related to joint cooperation in the Tumen River area and Northeast Asia and reached an agreement in principle for the lease of land by the three riparian states to an international

[24] "Tumen River Initiative"; *SUPAR Report*, no. 11 (July 1991), p. 30; Kaye, "Creative Tensions"; Lilley, "Travellers' Tales."

[25] UNDP, "Subregional Trade Development Leaves..." in the reports and documentation of the PMC Second Meeting held in Beijing in October 1992, p. 3.

corporation—the Tumen River Corporation (TRC). Shareholders in the TRC will also include public and private sector investors and Mongolia and the ROK who are full members of TRADP.[26] The corporation will oversee development in the three zones that now comprise TREZ, and according to the UNDP, will be an independent body with international management headed by a former executive of the giant U.S. engineering firm Bechtel.[27]

However, documentation from the PMC III reveals that TRC will exist within a complex matrix of institutional structures whose membership, interests and responsibilities have not yet been clearly defined or agreed to. The first two of the agreements referred to above established two new bodies including a coordinating committee from China, the DPRK and Russia to harmonize activities of the riparian countries in the TEDA called the Tumen River Area Coordinating Committee (TRACC). The second is a consultative body comprised of the five TRADP governments in NEARDA, which might eventually be open to other countries and institutions such as Japan, the ADB and the World Bank, called the Northeast Asian Regional Development Commission (NARDC).[28] Figure 2, which is expanded upon in the following paragraphs, illustrates the possible relationships between the various stakeholders, institutional structures and geographic regions for the Tumen River project in Northeast Asia.

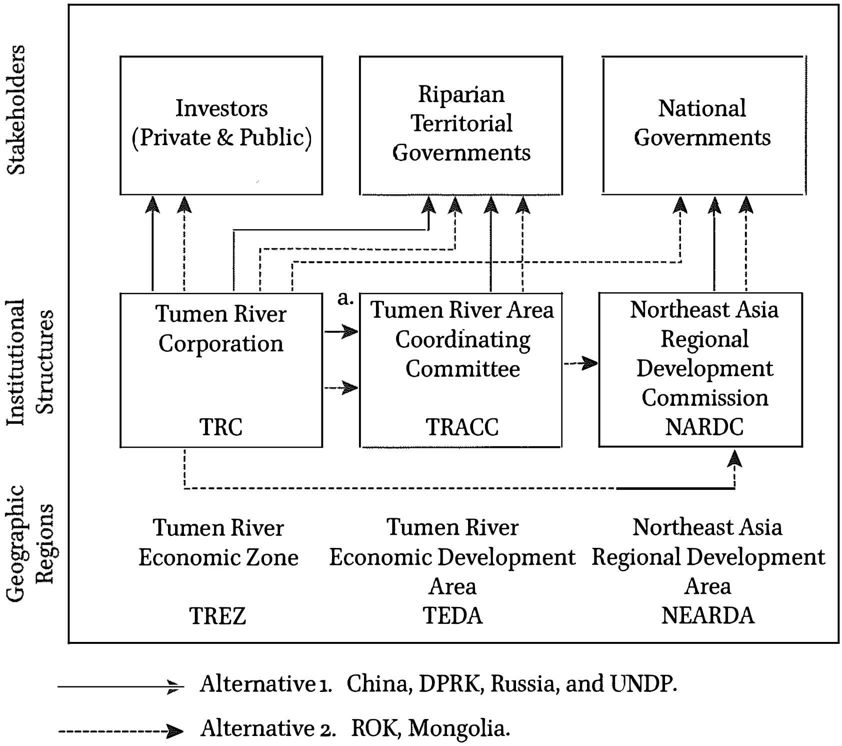
The functions of the Regional Development Commission (NARDC) would be to review, advise and approve TRADP plans from a regional perspective, but its relationship to the Coordinating Committee (TRACC) and the Corporation (TRC) seems to fall into at least two alternative arrangements—see figure 2. In the first, supported by the riparian states and the UNDP, NARDC would provide only "advice and guidance" to TRACC and TRC on issues such as economic policy, infrastructure, taxes, foreign exchange, concessions, regulations and the environment.[29] Under such conditions there would be no policy overview of TRACC, no reporting relationships from TRACC and TRC to NARDC and no supervision of TRC. The ROK and Mongolia, on the other hand, see a greater role for NARDC in establishing, approving and directing TRACC and TRC operations. Under

[26] "Tumen Triangle," p. 7; "Pact Inked on Lease of Tumen River Land," *China Daily*, 13 May 1993, p. 2.

[27] Clifford, "Send Money," p. 72.

[28] UNDP, *PMC III Reference Matrices Covering Institutional, Legal and Financial Issues*, Pyongyang (May 1993).

[29] Ibid., pp. 2–4.



[a] Socio-political issues only.

Figure 2. Tumen River Area Development Program.

this scenario both TRC and TRACC would report to NARDC which would establish investment priorities, operate common facilities, supervise TRC, coordinate dispute settlement, and coordinate environmental issues.

Similarly the riparian states' Coordinating Committee (TRACC) would function either independently or as a subcommittee of NARDC.[30] Although both alternatives call for the same membership (China, the DPRK and Russia) the first would, in addition to formulating and controlling the socio-political policy of TRC, also regulate flows of people, goods and capital, while the second alternative would elevate most issues as concerns for NARDC. Under this second alternative socio-political conflicts among the riparian states, for example, would be mediated by NARDC which would "deliberate" all noneconomic interests in TREZ.

30 Ibid., pp. 4–5.

Shareholders in TRC under the first alternative would be composed of the riparian states, based on land leasing, and investors, supervised by TRACC for socio-political issues only, and would be an independent corporate entity.[31] Its functions would include leasing land, managing property, borrowing money to finance development, administering the flow of labour, commodities and capital, and providing and/or coordinating the provision of physical, information and financial infrastructure. Under the second alternative all these functions would be directly supervised by NARDC, and shareholders would be expanded to include all full members of TRADP (i.e., same as the PMC). In other words Mongolia and the ROK would be considered as equal partners based upon their membership in the PMC.

Also mentioned in the PMC III documentation and worth highlighting briefly here are summaries of three other institutional, legal and financial issues.[32] First is a Tumen River investment code which recommends initial concessions for TRADP members designed for maximum investment attractiveness while at the same time attempting to reconcile the geopolitical issues described earlier. Based primarily upon the TRC's role within the first set of alternative institutional structures described above, the investment code provides the terms of reference for investment in production. These include access to markets, raw materials, labour, scientific and technical expertise, and a package of incentives such as advantageous royalty agreements, preferential import duties, tax holidays and a regulatory environment that is supposed to be "fair, firm and free from arbitrary interference." Second is a set of leasing terms for and characteristics of the TRC core city. Although the agreement will cover the entire region of TEDA from Vladivostok in Russia to Yanji in China to Chongjin in the DPRK the initial development efforts will focus on a limited core area plus appropriate port and other transportation facilities requested by the TRC and agreed to by the riparian leasees. The recommended length of the leases is seventy to one hundred years. Third is a set of alternative recommendations on currency and banking options in the areas to be leased by the TRC. The most favorable option according to the reports is one in which both convertible and riparian currencies circulate. Other alternatives discussed were the creation of a new currency or the possible circulation of the three riparian states' currencies.

Dialogue among participants of the UN-sponsored working groups and the PMC regarding institutional structures for TRADP collectively embody

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[31] Ibid., pp. 5–9.
[32] Ibid., pp. 10–18.

all the profound complexities and tantalizing opportunities for Northeast Asian regional economic cooperation. Originally conceived of by scholars at the East-West Centre the Tumen program was quickly adopted by the UNDP which has, since 1991, played a central role in coordinating and financing the multilateral negotiations, feasibility studies, and project promotion. Interestingly the UNDP has consistently sided with the institutional and other proposals supported by the riparian states apparently less concerned about the interests of the other full TRADP members.[33] Thus, the UNDP has supported institutional arrangements that assuage the concerns of China and Russia who are managing highly transitional economies, and the DPRK who, although desperate for foreign (Western) investment, remains deeply apprehensive about the geopolitical ramifications of the project.

Recent developments in the Tumen River area illustrate the practical implications for regional cooperation.[34] The ROK is considering a multi-million dollar soft loan to China to finance infrastructure improvement along China's border with the DPRK if Pyongyang fulfils its international obligations including International Atomic Energy Agency inspections of suspected nuclear sites. A leading ROK conglomerate has also agreed to finance, via a Chinese company, the reconstruction of a railway link between China's Hunchun to the DPRK Rajin-Songbong special economic zone and to finance development of Rajin port. Many interests are served if the investment proceeds: the DPRK is forced to consider the economic implications of its nuclear belligerence; China would gain a trade route to the Sea of Japan; the DPRK hopes the linkage to China's booming hinterland will draw foreign investors to its special economic zone; a South Korean firm hedges its exposure to risk by making its initial direct investment in the North through a Chinese company; and presumably it would spur Russian investment in complementary development on its side of the Tumen River.

Conclusions

Whether the developments noted above at the level of TRADP are signals of likely increased cooperation to promote regional integration at

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33 It was made clear during interviews with UN officials in Beijing that the UNDP would stay involved with the project only if the three riparian states continued to show interest in multinational cooperation.

34 W.B. Kim, "The Korean Peninsula and the Future of Northeast Asia," in S. Sekiguchi and M. Noda, eds., *Prospects of Economic Cooperation in East Asia* (forthcoming); and E. Paisley, "White Knights," *FEER*, 3 March 1994, p. 46.

the larger level remains to be seen. However, the potential for growing economic integration is considerable and is now recognized by trading partners outside the region. For example, in the last five years the Australian government has commissioned two major reports on the region (see Garnault, 1989 and Commonwealth of Australia, East Asia Analytical Unit, 1992) which have provided the basis for accelerated efforts by the Australian government to increase its economic presence in the region. It is therefore no less important that Canada, as well as other trading partners, recognize the potential of the region.

Direct participation of five nations with Japan as an observer in the Program Management Committee constitutes the first intergovernmental organization linking these countries to achieve economic cooperation and coordinated development in Northeast Asia. If for no other reason than this the Tumen River program is a (limited) success. Details of the institutional structure of TRADP are of major importance to studies, consultations, and subsequent negotiations leading to a formal agreement. The various institutional "options" currently being explored by participants reveal much about the complex economic imperatives and the realpolitik of Northeast Asia. Current agreements are for each country to maintain sovereignty in its own jurisdiction with no surrender of individual rights to a supranational organization.

The various UN missions to the region found overall support for TRADP to be striking in all participating countries although motives, interests and priorities are not identical. Desire for the development of the Tumen delta as a gateway to increased trade and economic integration within the subregion is general and has produced a certain political resolve. The fact that PMC III occurred at all in May 1993, amidst the DPRK's threatened withdrawal from the Nuclear Non-Proliferation Treaty, the ROK substantially withdrawing trade credits to Russia, and other deeply felt animosities, is a credit to the capacity of the project to bridge concerns. In this sense, TRADP has become both a symbol and a practical means for pursuing normalization and economic integration in Northeast Asia.

Since most of Northeast Asia has adopted export-led strategies for economic development, efforts to create a free-trading environment will be highly beneficial.[35] However, the development of other regional organizations requires that Northeast Asia seek cooperation as a region at once

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[35] See K.R. Kim, "Economic Co-operation in Northeast Asia: The Role of Korea," *The Korean Journal of National Unification*, special edition (November 1993), p. 176.

separate from the rest of the Asia Pacific region and integrated into a wider global economic community in the kind of open-regionalism PECC proclaims. Such multilateral arrangements will be necessary to manage the growing interdependence among the national economies and to deal effectively with certain issues such as environmental degradation. Here the intermediate-sized regional organizations such as APEC and PECC can serve as useful umbrella structures and forums for dialogue. PECC, for example, has actively promoted inputs from business and government and researcher exchanges of information in which regular contact and analysis of practical issues have evolved into effective transactional networks.[36] These activities could benefit from and build upon the dynamism of private-sector generated trade and investments, which in the region of the Tumen delta has been the effective driving force for Northeast Asian economic integration.

It is interesting to review the incredible changes that permit contemplation of a proposal that would have been unheard of even thirty-six months ago. The United Nations has committed several million dollars for feasibility studies and there is increasing interest in policy circles and the offices of multilateral agencies in examining the various possibilities. Despite particular national reservations, and contingent upon favourable cost-benefit analysis, it is just such an ambitious project like the Tumen River project that may provide the impetus around which ailing economies in Mongolia, Pacific Russia, and the DPRK can integrate. It may also help to sustain the growth rates of China, South Korea, and even Japan into the twenty-first century.

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[36] Ibid., pp. 167–77; and Pacific Economic Co-operation Council, *Pacific Economic Development Report 1992–1993* (Singapore, 1992), p. 16.