


The Prospect of AIIB's Potential Investment in North Korea and Its Implications



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With the successful holding of the inter-Korean summit and North Korea–US summit in the first half of 2018, discussions on the complete denuclearization of North Korea and subsequent economic compensation to North Korea are actively underway. Considering the enormous cost of developing North Korea and the various risk factors associated with financing this development, it is now necessary to seek various ways to finance this development more effectively. In this context, interest is growing on how the Asian Infrastructure Investment Bank (AIIB), led by China to solve the relative shortage in supply against demand in the Asian infrastructure sector, will be able to participate in North Korea's development following its denuclearization.¹

According to the articles of the AIIB, it can support the North Korean project using a non-membership countries track. However, the AIIB's investment in North Korea must go through a series of "not impossible, but very difficult" processes, since investment in North Korea involves a

¹ Lee, Hyuntai and Kim, Junyoung. 2018. "The Possibility of Asia Infrastructure Investment Bank (AIIB) to finance DPRK and its implication", *Journal of Contemporary China Studies*, Vol. 20, No. 1, pp. 153-181. (in Korean)

high risk and the AIIB is more of a commercial bank than other MDBs. The process would follow the following steps: first, the irreversible denuclearization of North Korea and the cancellation of sanctions against North Korea; second, risk assessment of investment projects and the confirmation of profitability through cost-benefit analysis; third, discussions with the board of directors and acquisition of a super majority at the general meeting; fourth, verification of North Korea's willingness to actively cooperate. A wide range of stakeholders including the AIIB, the two Koreas and the international community will need to spend a great amount of time and effort throughout all of these processes.

When considering the characteristics of the existing projects of the AIIB, if development investment projects actually commence in North Korea, the AIIB is likely to ① support a "project preparation special fund" for exploring and investigating infrastructure projects in North Korea, ② co-finance sovereign-backed projects with other MDBs, and/or ③ establish a "North Korean infrastructure development fund" to attract private capital both from home and abroad and invest this in North Korea. In light of the AIIB's emphasis on the participation of private capital, AIIB investment in North Korea can be expected to proceed in the manner of gradually increasing private investment through various channels of development funds. In addition, the AIIB's initial investment projects will likely be cross-border cooperation infrastructure projects in which AIIB member countries (Korea, China, Russia) and North Korea can all share common interests. On the other hand, it may be possible to invest in transportation infrastructure projects such as roads and railways in line with the "New Economic Map of the Korean Peninsula." We can also expect to see joint investments by the AIIB and private capital if investment conditions improve, as the risks associated with North Korean investment projects decrease and steady profits are generated.

If the AIIB is to overcome these numerous difficulties and take part in North Korean development projects, this would hold great significance for both North Korea and the AIIB. From the perspective of North Korea, participation on the part of the AIIB, the major MDB in Asia, carries the symbolic significance of promoting the importance of North Korean development to the international community and encouraging participation by various international investors. As for the AIIB, if it is able to successfully manage the risks associated with North Korea's internal political system and profitability issues, and actually conduct these business projects, it will have firmly established itself as Asia's leading MDB while greatly enhancing its internal capabilities in the areas of project selection, management and execution. In other words, investment in North Korea is an opportunity for the AIIB to widen its portfolio from Southeast Asia and Central Asia and begin full-fledged infrastructure development projects in the

Northeast Asian region, as well as to establish itself as the international financial institution leading the development of North Korea.

If the North Korean regime carries out measures toward irreversible denuclearization and North Korean sanctions are lifted, the Korean government should make efforts to upscale AIIB investment in North Korea and help it gain membership to international financial institutions. While North Korea's demand for development funds is enormous, the funds that can be mobilized from the Korean government and international community fall far short of this demand, meaning it will be necessary to actively support the AIIB's investment in North Korea. At the same time, however, and despite domestic expectations for rapid progress, the AIIB's investment in North Korea will require a sustained effort over the long term and calls for a steady approach. In particular, it is necessary to develop a strategy that will attract the interest and support of neighboring countries to participate in AIIB projects, by recognizing and actively communicating how North Korean development is beneficial not only to North Korea but also to the Northeast regions of China and the Russian Far East. The government could diversify funding channels by supporting North Korea's membership in the IMF, WB and other international financial institutions as soon as possible. In the long run, it will be necessary to pursue diverse efforts to attract public and private capital for North Korea's development from domestic and foreign financial markets, for instance through the establishment of regional development financial institutions such as the Northeast Asian Development Bank. **KIEP**