

Negotiating a Korean Settlement: The Role of Sanctions

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Coordination problems or “weak links” have prevented the imposition of a robust sanctions regime vis-à-vis North Korea. As North Korean testing has accelerated, the US, Korea and Japan have responded to this problem by seeking to engage China on the issue, by deploying secondary sanctions, and by trying to curtail trade and financing with other parts of the world. Yet despite the emphasis placed on sanctions, North Korea appears to favor direct material payoffs to sanctions relief and at present seems largely uninterested in negotiations on the nuclear issue.

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A handful of sanctions advocates believe that they can “work” either by forcing unilateral policy changes on the part of North Korea or even forcing regime change. Yet most proponents of sanctions under-

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stand that they play a more complex role in denuclearization: that they grant leverage precisely by the promise to lift them in return for a negotiated quid-pro-quo. This source of leverage is true of secondary sanctions as well, although with the complication that market actors ultimately need to change their behavior if sanctions relief is to have effect.

The Iran negotiations demonstrate these dynamics. Sanctions — including secondary sanctions — clearly moved Tehran toward negotiations; it can hardly be argued that they didn't work. But the interim Joint Plan of Action concluded in November 2013 provided Iran with limited and temporary sanctions relief. The final Joint Comprehensive Plan of Action (JCPOA) reached in July 2015 contained an intricate roadmap culminating in the lifting of the most significant multilateral sanctions on Iran, but by no means all bilateral ones.

Yet getting from here to there is by no means straightforward, primarily because of the time inconsistency and coordination problems in negotiating such settlements. Using inducements to achieve political objectives raises difficult sequencing problems. If the inducements are offered and granted first, the target may subsequently have little incentive to cooperate. Critics of North Korea have long focused on the moral hazard problems associated with engagement (Eberstadt 1999; Bolton 2007). In his memoir, George W. Bush (2010) recounts a March 2001 meeting where he decided that the basic mode of dealing with North Korea would change: "From then on, North Korea would have to change its behavior *before* we made concessions" (emphasis in the original). This conception of sanctions relief — that North Korea would need to move first — undergirded the Obama administration's strategy of strategic patience, which is frequently deemed a failure (for example, Council on Foreign Relations 2016). It should be noted, however, that the JCPOA was significantly front-loaded as well, placing wide-ranging demands on Iran before sanctions relief could begin.

Yet the opposite problem also exists. If the economic inducement of lifting sanctions is made conditional on some action and promised only in the future, the sanctioning state has the credibility problem.

Will it deliver on its promises? Can it reverse the effects of secondary sanctions? And will it have incentives to deliver on promises if the target state takes actions that are not easily reversible, such as dismantling its nuclear capability? Note that these dilemmas are more intense for a state that has already developed weapons such as North Korea than for a state like Iran that is only a latent nuclear power, since usable rather than potential military assets would be foregone.

Histories of negotiations with North Korea demonstrate repeatedly that such time inconsistency or sequencing problems can generate a very narrow conception of reciprocity that in turn creates second-order bargaining problems (Funabashi 2007, Chinoy 2008, Haggard and Noland 2017, Chapters 6 and 7). In the favored terminology of the North Koreans, negotiations require “words for words, actions for actions.” The result, however, is that the concessions to be exchanged are sliced into finer and finer tranches. Exchanges may be made more comparable and less time inconsistent, but, as in Zeno’s dichotomy paradox, the ultimate goal is never reached.

Precisely because of these difficult negotiating problems, “grand bargains” have periodically been proposed that cut through them by putting everything on the table at once. Because these various goods cannot be delivered on similar schedules — in part for physical reasons, such as the time to build a light-water reactor — grand bargains do not altogether solve these problems. Time inconsistency problems in implementing the agreement would persist.

A second well-known issue in using sanctions is the coordination problem (Martin 1992, Hufbauer et. al. 2007), and it is on ample display in the North Korean case. Sanctions are clearly more efficacious when major trading partners are able to coordinate around them or can rely on secondary sanctions to deter private actors from economic exchange. If they are unable to do so, then trade will simply be diverted from sanctioning states to those more willing to accommodate the target.

These coordination problems not only affect sanctions but the offering of inducements as well. If target states are able to rely on forgiving trade partners, then the benefits on offer from the sanctioning states — and their bargaining power — are correspondingly reduced.

China has played this patronage role in the Korean case, leading to perverse effects. As the sanctions regime against North Korea tightens, its trade has simply become more and more concentrated on China.

In sum, the answer to whether sanctions relief will play a role in any final settlement of the North Korean nuclear deal is relatively clear. Except for those holding out for unilateral concessions, regime change, or military solutions to the North Korean conundrum the answer is “yes.” But even for those recognizing that sanctions will ultimately be relaxed, the question of “how” poses three issues, and they will structure the remainder of this essay:

- Should — and can — sanctions be tightened first to generate more leverage in subsequent negotiations, including through more aggressive use of secondary sanctions? This option has to be considered in some detail, since it is quite clearly the policy track on which the US, South Korea and Japan have embarked under the Obama, Park and Abe administrations. Moreover, it is likely to be continued — at least initially — under a Trump administration. Answering this question requires a consideration of the Chinese role in the sanctions regime and whether secondary and other sanctions might have an effect on it.
- Second, in the context of the existing sanctions regime, is it possible to consider an interim solution such as a freeze? What role might sanctions relief play in such an agreement?
- Finally is the question of what role sanctions relief and broader economic inducements might play in a final settlement. Although currently quite distant, this question needs to be posed. It is not entirely clear whether the economic inducements of sanctions relief — promising a broader economic opening — is of any interest to the leadership in Pyongyang; indeed, such opening could be seen as threatening. Rather the regime favors transfers of essentially fungible resources that can be used at its discretion.

I conclude that there is value in tightening the sanctions regime first, but only in the context of a wider offer to put all issues on the table. A freeze can be a part of such a deal. But given political con-

straints, a freeze is highly unlikely in the absence of a broader framework that commits the parties to denuclearization and a final political settlement. Such a settlement would not only include some phased lifting of sanctions but security assurances or guarantees and other economic inducements as well.

I am skeptical, however, that the North Korean regime has an interest in denuclearization at this point, given how advanced its nuclear weapons and missile programs are. As a result, even if the United States were to cooperate with China in making the broad offer suggested here, we are entering a period likely to be characterized by a “two-track” or containment strategy in which such offers will be made but with declining expectation that they will yield fruit.

I. The Current Sanctions Regime and the Political Economy of North Korean Trade

The sanctions regime facing North Korea has two components. The first is multilateral and tied directly to the country’s nuclear and missile program. The second component is a complex welter of bilateral sanctions, most notably from the United States, Japan, and South Korea. These bilateral sanctions go beyond the multilateral ones associated with the nuclear and missile programs, targeting the country for a variety of other reasons: punishing military actions in the case of South Korea, abductions in the case of Japan, and human rights violations and trade in illicit goods in the case of the United States. The Iran negotiations suggest that any final deal with North Korea would focus first on multilateral sanctions relief. A crucial question is whether that would be adequate to provide North Korea significant relief and the answer — in contrast to Iran — could well be “no.”

The reasons are to be found in the nature of the multilateral sanctions regime and the goods it has targeted. Multilateral sanctions have been imposed since mid-2006 in response to missile but primarily nuclear tests. These have been contained in UN Security Council resolutions: UNSC 1695 of July 2006, UNSC 1718 of October 2006, UNSC

1874 of June 2009, UNSC 2094 of February 2013, UNSC 2270 of March 2016 and UNSC 2321 of December 2016. The details of these sanctions have been outlined elsewhere (Haggard and Noland 2017). It is sufficient to note here that, because of the Chinese veto on the Security Council, the sanctions were initially defined relatively narrowly around WMD-related matériel and major weapons systems.¹ The gradual introduction of complementary multilateral sanctions on financial flows and aid in later resolutions was similarly tied to WMD and weapons-related activities and did not, in principle, affect the financing of commercial trade.

Not until 2016, with UNSC 2270 and 2321, was commercial trade targeted directly for the first time, most notably in the form of a ban on coal exports in 2270 that would have had significant effect if fully implemented and a cap on coal exports contained in 2321 that would appear to have significant material effect. But Chinese implementation of UNSC 2270 has been lax to date, reflecting major loopholes that China effectively wrote into the resolution, and thus its commitment to fully implement 2321 remains in question.²

Despite limits on their scope, there are three reasons that these multilateral sanctions may have broader effect, on trade and investment with North Korea, quite apart from the costs imposed by any additional bilateral sanctions. First, the multilateral sanctions were accompanied by other forms of collective enforcement. Inspection and interdiction activities were conducted not only under the aegis of the UN resolutions but through the US-led Proliferation Security Initiative (PSI) as well. Second, UN Security Council resolutions gradually came to include prohibitions on dual-use technologies, some of which might have been imported for purely commercial rather than military purposes. Restrictions on dual use technologies can have commercial as well as military effects. Finally, in addition to their direct impact on arms and luxury goods, sanctions may also drive up the risk premium

1. There was also a weakly enforced ban on luxury good exports.

2. Most significantly is a “livelihood” exemption if the sanctions are deemed to have adverse welfare effects and the requirement that earnings be tied directly to WMD programs.

on all exchange with North Korea by introducing uncertainty and deterring commerce in areas not directly subject to them.

These last effects are the hardest to gauge, but profoundly complicated negotiations over sanctions relief. North Korea appears to believe that its foreign economic relations are shaped primarily by sanctions. But it is highly plausible that the steady decline in North Korea's trade with the world outside of China is also the result of perceived risks generated not only by its nuclear and missile program but by its notoriously weak protection of property rights and contract. If trade is falling because traders and investors have no confidence in the regime's economic policies, then lifting sanctions could have scant material effect.

The bilateral sanctions regime is much more complicated precisely because it is the result of idiosyncratic factors in each country. The important point to note is that the countries inclined to sanction North Korea either have had negligible economic exchange with it (the United States) or have seen the significance of their economic ties shrink as a result of bilateral sanctions.

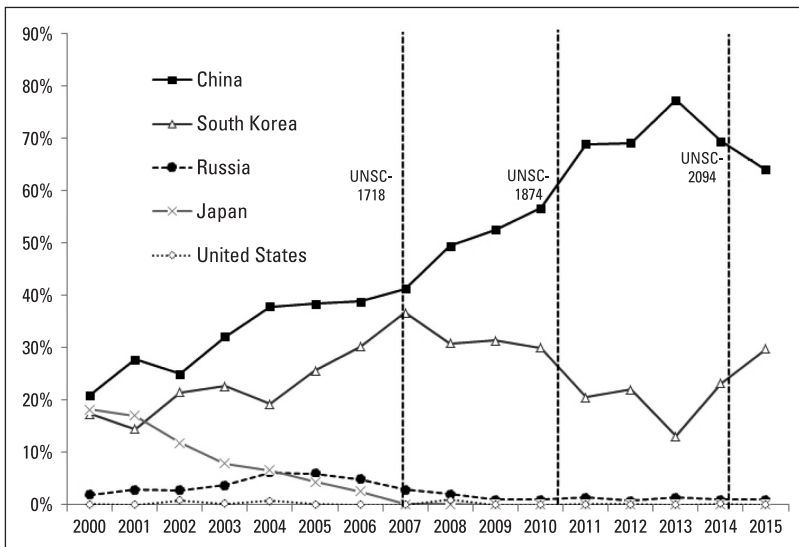
For the United States, there has long been little scope to further curtail direct commercial trade and investment as there was little to begin with. South Korea and Japan have increasingly faced similar dilemmas since the onset of the nuclear crisis. North-South trade began to fall with the transition from pro-engagement governments in the South to the administrations of Lee Myung-bak (2008-2013) and Park Geun-hye (2013-present) and the decline in assistance. Sanctions imposed following the sinking of the *Cheonan* virtually ended bilateral trade outside of the Kaesong Industrial Complex, and that too was finally shut down following the fifth nuclear test in 2016. After the onset of the nuclear crisis in 2003, Japan also drifted toward a virtual embargo on trade with North Korea.

The direct and indirect effects of the multilateral sanctions regime, the effects of bilateral sanctions and the persistent perception of North Korea risk on the part of private actors can be seen in Figure One below, which shows the share of five-party trade with North Korea through 2015. As can be seen, trade with the United States has

consistently been minimal, and Russia has not emerged as a backstop for North Korea because of financial constraints and lack of complementarities. What is striking is how the sanctions-related decline in Japanese and South Korean trade is more than made up by the steady deepening of North Korea’s economic relations with China. China’s share appears to drop marginally in 2014-15 as Kaesong was reopened following its closure for part of 2013. But as of 2016 — with the closure of Kaesong — trade with the South has essentially fallen to near-zero levels. Bilateral trade with China could account for as much as 90 percent of North Korea’s total trade even if total trade flows have trended down gradually since 2014 as a result of the slowdown in China’s growth.

Several conclusions emerge from this consideration of the current sanctions regime. First, although sanctions alone are not the only factor in the changing geography of North Korea’s foreign trade, they

Figure 1. Share of DPRK Total Trade with Six-Party Talks Partners



Note: (1) 10 percent CIF/FOB conversion applied to values reported from partner countries; (2) includes inter-Korean trade designated as “non-commercial” by MOU.

Source: KOTRA North Korea Foreign Trade Trends (various issues), Ministry of Unification Major Statistics Inter-Korean Relations, UN Comtrade, Authors’ Calculations.

appear to have had the perverse effect of pushing North Korea towards greater dependence on China. The focus on China's willingness to use the leverage which it quite obviously has is thus fully warranted. Second, it is also the case however that the very decline in trade and investment with other countries provides the opportunity for benefits were those sanctions lifted. This is true, however, only under the assumption that the decline in trade is directly or indirectly related to sanctions. While this is obviously the case for North Korea's trade with South Korea and Japan, it may be less true for trade with the rest of the world or in the gradual slowdown with China, where more general perceptions of risk no doubt pertain. Moreover, as I will argue in more detail below, it is not clear that the regime has an interest in a general opening to trade and investment, as it has historically sought more direct transfers that the regime can directly control.

II. More Sanctions to Get to Less?

Critics of sanctions, both in general and with respect to North Korea, frequently argue that they do not "work." However, this claim can mean two, quite different things and it is important that they be separated. The first is that certain regimes such as the North Korean one are so authoritarian and repressive that they are capable of resisting any sanction that is imposed. The costs of sanctions are simply passed on to the hapless population while the elite can shield itself from the costs. Often cited in this connection is the fact that the regime was able to withstand the great famine of the mid-1990s — in which 3 to 5 percent of the population perished — but nonetheless emerged largely intact.

Yet on reflection, this claim about the capacity of North Korea to withstand sanctions is almost certainly wrong. It is possible that a completely autarkic agrarian economy might be able to withstand a complete embargo of its external economic relations, although at extraordinary cost. But North Korea has never fit that picture, pretensions of *juche* and self-reliance notwithstanding. During the Cold War,

North Korea was heavily dependent on inputs from the Soviet Union and trade with the Eastern bloc countries. Since the end of the Cold War it has not only become increasingly dependent on China but more open as well: foreign trade is accounting for an increasing share of GDP.

This increasing openness suggests that North Korea has become more, not less vulnerable to sanctions over time. It is unimaginable that North Korea's foreign policy would remain unchanged if it was cut off from its trade with China entirely, particularly given the fact that it continues to rely on its patron for imports of both food and fuel and for exports of core commodities such as coal. Greater Chinese restrictions on North Korea's commercial trade might not generate a change in regime, but we can certainly imagine them producing balance-of-payments constraints and even a financial crisis, the mechanics of which are well-known.³

The second meaning of the claim that sanctions "don't work" is much more plausible and has been a staple of the analytic literature on sanctions for some time (for example Martin 1992, Hufbauer et. al. 2007). This second meaning is that sanctions cannot work vis-à-vis North Korea because the coalition of countries required to impose them with adequate force has weak links. Note, however, that this is actually not a claim that sanctions "don't work"; it is a claim that they are not being implemented. As Figure 1 shows, it appears that it is this second meaning of "not working" that is in play in the North Korean case. Sanctions have faced profound coordination problems, China has been willing to sustain commercial relations with the country, and as a result North Korea has not fully paid a significant economic cost for its foreign policy behavior.

3. Signals of balance-of-payments distress would begin with North Korean importers seeking lengthened settlement terms and a drying up of credit (Fifield 2016). This would be followed by a depreciation — probably rapid — of the black market exchange rate for the won and a rise in prices of basic commodities, including rice, in North Korea. Although some North Korean exporters might gain, imports of intermediates, bulk commodities such as food and consumer goods would suffer.

Before we can answer the question of what role sanctions might play in a negotiated settlement we therefore have to ask the question of how to strengthen the sanctions regime against North Korea as a prelude to loosening it. This might occur in one of three ways. The first is to convince China that its strategic interests are best served by acting more forcefully against the country. The second is for the interested parties, led by the United States, to impose secondary sanctions that would indirectly limit China's trade, investment and financial relations with North Korea. The third would be to go after the residual trade that North Korea does with countries outside China, including in new activities such as labor exports. Although the prospects of any of these options remain uncertain, they have not been foreclosed. Some of these efforts are already in train in the United States, South Korea, Japan and Europe. What are the prospects for their success?

A. Convincing China to Do More

The idea that China must "do more" with respect to North Korea has now become a virtual staple of American political discourse on the issue, reflected not only in the presidential campaigns of both Donald Trump and Hillary Clinton but in prominent US policy reports (for example, Council on Foreign Relations 2016). China has been consistent in its stated opposition to North Korea's nuclear program and has signed on to multilateral sanctions through the UN Security Council.

However, the broad evidence to date — visible in the trade data cited above — is that China remains extremely reluctant to exercise much greater economic leverage over the regime in Pyongyang than it has to date. Indeed, Beijing appears to favor a "deep engagement" approach to North Korea (Reilly 2014a, b).

The balance of reasons for China's reluctance to more is ultimately unknown, but the candidate list is obvious and no doubt reflects the interests of different tendencies within China's foreign policy establishment (International Crisis Group 2009). At the "harder" end, some strategic thinkers believe that the continued existence of North

Korea is preferable to a unified Korea and the greater proximity to the Chinese border it would allow for American and ROK forces. Yet even short of such a view of North Korea as a strategic asset, China faces a host of other prudential concerns about applying pressure, from the general uncertainty such pressure might bring, to the effect on provincial economic interests and the risks of large population movements were the North Korean economy to unravel quickly.

Chinese declaratory policy also reflects a reluctance to press North Korea. Although opposed to North Korea's nuclear program, China's declaratory policy also includes two other components: a commitment to settling all relevant issues through negotiations and maintaining "peace and stability" on and around the peninsula. From China's response to particular provocations, it is clear that the meaning of maintaining "peace and stability" includes opposition even to deterrent and defensive reactions to North Korea's provocations and a preference for the "stability" of the Kim regime itself.

During the trilateral summit with Korea and Japan in August 2016, Foreign Minister Wang Yi subtly modified Chinese policy to include "three objections," including a stated opposition to North Korea's effort to develop missiles with the capacity to deliver nuclear warheads. But in addition, he also opposed any "remarks and actions" that will trigger tension on the Korean Peninsula and all measures that "violate" the United Nations Security Council Resolution 2270. These latter two conditions underline resistance to any military moves on the part of the US, South Korea and Japan including the deployment of defensive systems such as THAAD (Terminal High Altitude Area Defense), to which the United States and South Korea committed in July 2016. Minister Wang Yi's statement could also be read as opposition to sanctions which go beyond those outlined at the multilateral level.

Prolonged negotiations over a new sanctions resolution following the sixth test showed that China was willing to agree to some adjustments to the sanctions regime, most notably in a harder cap on coal exports. But hopes that China will take any actions that might put the North Korean regime at risk probably remain in the realm of wishful

thinking. If China was to “do more,” it would almost certainly be through a diplomatic initiative that would require concessions on the part of the United States and South Korea as well. We return to what such an arrangement might look like below.

B. Secondary Sanctions

Under legislation passed in early 2016 and important executive orders (EOs) that followed, President Obama was granted quite substantial authority to impose secondary sanctions. In outlining possible targets for secondary sanctions, E.O. 13722 includes firms dealing with any industry that might be designated (“such as transportation, mining, energy, or financial services”); companies engaged in trade in metal, graphite, coal or software, broadly in line with UNSCR 2270 and 2321; entities engaged in facilitating human rights abuses or censorship; entities engaged in labor exports; and firms undermining cybersecurity. Yet the two dozen designated entities and persons under the EO include some ships, banks and trading companies and regime personnel — including Kim Jong Un himself — all of which are highly unlikely to fall under American jurisdiction any time soon.

Two more recent developments have made the prospects for more aggressive secondary sanctions much more plausible looking forward, however. First, two important reports published in 2016 (Park and Walsh 2016; Center for Advanced Defense Analysis 2016), using both extensive interviews and network analysis, showed how North Korean firms have managed to circumvent sanctions by relying on Chinese brokers. These large, more sophisticated Chinese intermediaries not only provide a veil of protection for North Korea’s state trading companies when dealing with a variety of third parties. They also handle logistics constraints made more pressing by the multilateral sanctions regime. Moreover, the size of these brokers allows them to effectively provide trade financing for North Korea, financing that it could generally not secure through banking institutions that are increasingly falling under sanction. These firms also effectively permitted North Korea’s state trading companies to extend their net-

works into Hong Kong and Southeast Asia, aided and abetted by ongoing embassy involvement in sanctions circumvention.

The Center for Advanced Defense Analysis report proved particularly influential as it provided extensive open-source evidence on the operations of a single group. The Dandong Hongxiang Industrial Development Co. Ltd., a subsidiary of the sprawling Liaoning Hongxiang Group, had its hand in over \$500 million in trade with the DPRK from January 2011 through September 2015, over half of it in coal. While North Korea's Foreign Trade Bank had been sanctioned under a US executive order in 2013, Hongxiang was nonetheless able to do business with the bank and was probably trading in proscribed dual-use technologies as well.

The US Justice Department moved quickly in response to the report, indicting top managers of the firm outright for sanctions violations, conspiracy, and money laundering. In addition, Justice actions included a civil forfeiture case that went after Dandong Honxiang's accounts, which were held by top Chinese banking institutions. Chinese authorities also moved against this firm on grounds of corruption, suggesting some of the outer limits of Beijing's patience.

The second initiative undertaken by the United States in 2016 was the designation of North Korea as a jurisdiction of primary money-laundering concern. Such designations are frequently confused with a sanction but in fact they operate differently. The ruling requires American banks to exercise due diligence that their counterparties are not conducting sanctioned business with North Korea. In 2007, a similar designation against a single bank — Macao-based Banco Delta Asia — triggered a run on the bank. Although conservatives seeking regime change favored the measure, the United States ultimately settled the BDA case in order to bring North Korea back to the Six Party Talks.

It is too early to judge whether these secondary and financial sanctions will have similar effects, and there is ample room for doubt. North Korea might be able to shift banking business to weakly-regulated jurisdictions — including Iran — or to small, weakly-regulated banks elsewhere. Small regional or municipal banks in China

may not need access to the US financial system, and may be willing to tolerate borrowed-name accounts opened by Korean Chinese on behalf of North Korean entities. Yet running an economy the size of North Korea's on cash is ultimately unsustainable, and it is plausible that such financial measures will ultimately have at least some economic effect on North Korea, further narrowing the geographic scope of its foreign trade and investment.

C. Squeezing Trade and Investment from the Rest of the World

As figure 1 implies, North Korea's trade with the rest of the world has fallen dramatically and access to finance from the world outside China is virtually non-existent. Nonetheless, there is probably some room to go after new foreign exchange earning strategies that North Korea has pursued, for example with respect to labor exports and even military cooperation with smaller states in Africa and elsewhere. Such efforts do not necessarily entail the use of secondary sanctions, but diplomatic efforts to convince North Korea's trading partners to exercise due diligence. A number of core measures in UNSC 2321 were aimed at reducing the ability of North Korea to conduct business abroad, and particularly through its embassies.

D. More Sanctions? A Reprise

The preceding review of sanctions options is important because it is at least plausible that they might work. China has not just been reluctant to impose tougher sanctions on North Korea. Even when negotiating multilateral sanctions China has simultaneously served as a partner of last resort. But a significant share of Chinese trade is ultimately commercial and if North Korea is squeezed elsewhere — as it has been most recently by the closing of Kaesong — then it loses access to foreign exchange that has been used to finance its current account deficits with China. Although there is uncertainty about the effects of secondary sanctions, designation of North Korea as a juris-

diction of money-laundering concern could well cumulate into pressures that North Korea has not seen in the past. For these reasons, it is unlikely that the sanctions option will simply be set aside. But could it be in the presence of some sort of interim or permanent deal?

III. Sanctions and Inducements in an Interim Agreement

During 2011 the United States pursued a softening of strategic patience through the negotiation of a “food for freeze” deal. The agreement was finalized just before Kim Jong-il’s death on December 17, 2011 and announced publicly on February 29, 2012; it thus became known as the Leap Year or Leap Day deal. North Korea agreed to implement a moratorium on long-range missile launches, nuclear tests and nuclear activities at Yongbyon, including uranium enrichment as well as reprocessing activities. The DPRK also agreed to the return of IAEA inspectors to verify and monitor the moratorium and confirm the disablement of the 5-MW reactor and related facilities.

In return, the United States made declaratory statements that it had no hostile intent toward North Korea, that sanctions were not aimed at the North Korean people, and that it would be willing “to improve our bilateral relationship in the spirit of mutual respect for sovereignty and equality.” Yet it is clear that the key concession on the US side was the offer of a very substantial aid package of 240,000 metric tons of food aid. Despite the fact that the United States denied that there was any linkage between the two, such linkage was in fact quite obvious.

The Leap Year Deal fell apart almost immediately with the announcement by Kim Jong-un of the intention to launch a satellite that was seen as a thinly-veiled missile test. Although the test failed, it set in train a sequence of events that bore an uncanny similarity to those following the second nuclear test in 2009: international condemnation and imposition of additional sanctions; a second, more successful satellite launch in December 2012; another expression of multi-lateral concern and sanctions; a third nuclear test in April 2013; a third

UNSC sanctions resolution; and one of the most taut periods of military confrontation on the peninsula in the spring of 2013.

Several features of the Leap Year agreement are of interest to the discussion of the role that sanctions relief might play in reaching an interim agreement with North Korea. First, it is wrong to say that Obama administration was unwilling to consider strategic concessions, including economic ones. The United States understood full well that substantive quid-pro-quo would have to be offered to secure North Korean compliance. After a decent interval from the sinking of the Cheonan and shelling of Yeonpyeong island, the United States was willing to consider an interim arrangement with little explicit linkage to a wider framework or resumption of the Six Party Talks. But it is also the case that the failure of this agreement cast a long shadow over the willingness of the Obama administration to revisit such arrangements. The North Korea issue moved to the back burner.

Second, it is noteworthy that the quid-pro-quo of the Leap Year deal did not entail sanctions relief, but rather a more direct transfer to the regime of fungible resources. Despite the continual mention of sanctions as an impediment to trust-building, it is not clear that any marginal lifting of bilateral sanctions by the United States — or even by South Korea and Japan — would provide enough assured resources to the regime to make such a deal attractive.

There have since been several proposals that the United States should revisit the idea of a freeze as an interim trust-building measure, and it is striking that few focus on sanctions relief. At the “hard” end of such approaches, a recent Council on Foreign Relations task force report suggests an interim freeze agreement, but is exceedingly vague on what might be offered in return. Ideas mentioned include a return to food assistance and some modification of exercises, but equal if not greater emphasis is placed on the threat of additional sanctions. In a different variant of the freeze, Joel Wit (2016) suggests using North Korean concern about exercises as leverage. Heginbotham and Samuels (2016) reflect a subtle shift in the debate about the very locus of the discussion. Rather than discussing what might be on offer to North

Korea for an interim agreement, they focus on what might be offered to China in order to get Beijing to exercise leverage: freezing deployment of ground-based interceptors, scrapping THAAD deployment, providing financial assistance for refugees, or pledging not to station troops north of the 38th parallel in the case of unification. Interestingly, North Korea's most recent offer does not focus on sanctions relief either, but rather a series of steps the United States could make with respect to its own nuclear posture on the peninsula (KCNA 2016).

The reasons why sanctions relief figures so little in these proposals is due in part to the US, which sees sanctions and simultaneous inducements as complementary rather than contradictory. Although coming from very different orientations, both the CFR report and Wit's proposal argue for maintaining and even strengthening sanctions while simultaneously seeking some interim arrangement. But not enough attention has been focused on the fact that North Korea may not see any significant return from sanctions relief. First, North Korea has been able to muddle through despite sanctions because of its deepening ties with China. Second, the regime may recognize that sanctions relief will only have uncertain and delayed economic effects, and thus may not be as beneficial as is thought; indeed, as I argue below in more detail economic opening could even be threatening. Finally, North Korean perceptions might also be colored by the shift towards secondary sanctions. Since these instruments rely on the behavior of market players, their reversal does not reside entirely in the hands of the state that initiates them.

IV. Going for a Grand Bargain: The Role of Economic Inducements in a Final Settlement

Except for those betting on unilateral North Korean concessions or regime change — both unlikely prospects — most American policymakers and analysts understand full well that a final settlement on the Korean peninsula will involve a complex of inter-related quid-pro-quos. The Joint Statement of September 2005 has already outlined

the core elements of such a deal, and the agreement with Iran also demonstrates clearly that the United States understands the role of sanctions relief. The questions with respect to such a final settlement are three. First, what can the major actors do to move back toward negotiations on the issue and what role might sanctions and sanctions relief play in restarting negotiations? Second, what might such a final settlement look like? But finally — and casting a shadow over these first two questions — what interest does North Korea have in returning to negotiations at this juncture?

With respect to the first question, it is clear that the United States and China will play pivotal roles in any resumption of negotiations. North Korea — and China — have always insisted that the key to any agreement is an end to the “hostile policy” of the United States and a larger political settlement that would normalize relations. For its part, the United States has rightly underlined that China will need to play an active and engaged role in such negotiations, if for no other reason than its economic relationship vis-à-vis the North outlined above. Given that North Korea has completely rejected negotiations that focus on denuclearization and the United States has rejected the idea of negotiating a peace treaty prior to denuclearization, the compromise appears relatively clear: either to pursue parallel negotiations on denuclearization and a final settlement or roll all issues into one omnibus negotiation that puts everything on the table.

What might such a final settlement look like and what role might sanctions relief play in it? Despite the fact that negotiations are deadlocked, the broad outlines of a deal have been pretty well-known since the Joint Statement of 2005 and can be outlined briefly:

- A process leading to complete, verifiable and irreversible denuclearization (CVID) overseen by the IAEA;
- Terminating the state of war on the peninsula by replacing the armistice with a peace treaty and normalizing North Korea’s bilateral relationships with the United States and Japan.
- Such normalization would imply the end of any hostile intent among the parties, buttressed by security guarantees.

- A regularization of North-South relations.
- The end of multilateral sanctions associated with the country's nuclear program.
- The lifting or partial lifting of bilateral sanctions and provision of economic assistance.
- The creation of a larger security and/or economic architecture involving the four or six parties, which could include *inter alia* a nuclear free weapons zone, a free trade area or North Korean participation in other multilateral agreements including the China-led Asia Infrastructure Investment Bank.

It is beyond the scope of this essay to go into the details of how each of these components might emerge or function in equilibrium and there are no doubt others that might be considered. However, three comments are germane.

First, it is important to underscore that sanctions relief might initially be limited to the lifting of multilateral sanctions. The domestic political authorities governing sanctions in some of the countries in question — most notably the United States — are extraordinarily complex and contingent on progress on other issues. A recent review of the legal authorities in the United States under which economic relations with North Korea are constrained or controlled totals no less than 33 discrete legal measures (Resnick 2016) and this was before the complications that arise from more aggressive pursuit of secondary sanctions. Some of these authorities are directly related to nuclear proliferation and thus could presumably be lifted in the context of a wider agreement. But others are tied to North Korea's status as a communist state, human rights violations, the non-market nature of the North Korean economy and so on. Moreover, while some of these can be waived at the discretion of the president, others cannot and would require legislative action. Politics will thus come powerfully into play, as Congress might have different views than the president. This was case in the Iran deal, under which bilateral sanctions on Iran were actually tightened in the wake of an agreement that lifted multilateral sanctions. In differing degrees, such constraints might operate in

Japan — most notably with respect to abductees — Europe and South Korea.

Second, a complicated issue in any negotiations would undoubtedly center on the provision of economic assistance. In the 2005 Joint Statement, the Six Parties not only undertook the vague commitment “to promote economic cooperation in the fields of energy, trade and investment, bilaterally and/or multilaterally.” They also committed to the provision of energy, including a very precise amount of electric power from South Korea, as well as to assistance in providing the country with light-water reactors, as was done under the Agreed Framework of 1994. Needless to say, the provision of such assistance would involve hard bargaining.

Finally, it is worth noting that while South Korea in particular has periodically floated ambitious ideas about regional economic cooperation as an inducement for North Korea to come to the bargaining table or denuclearize, the North Korean regime has shown scant interest in such ideas. The main reasons is worth underlining: broad economic inducements that involve opening the economy to foreign trade and investment pose challenges to the regime as well as benefits. Despite Pyongyang’s recent drive to secure foreign direct investment, it is clear that the model undergirding these efforts is one in which the regime maintains control and is capable of directly attaching the resources that are associated with the economic activity in question. The Kaesong Industrial Complex provides an example.

V. Conclusion

Sanctions play a complex role in the current state of diplomatic play with North Korea. For the US, Japan and South Korea, the continuing imposition of sanctions is seen as complementary to the making of various offers to resume negotiations. Such “dual track” policies have a long history in diplomacy around the peninsula and are not likely to be given up altogether. To the contrary, the plausibility that such measures might have effect is resulting in a more rather than

less aggressive pursuit of such options, most notably in the form of secondary sanctions. While there is a recognition that sanctions relief will ultimately play a role in a final settlement, it is not clear that such an offer will play a central role in an interim agreement, which is likely to be cemented by broader political and military promises and tangible and direct economic assistance.

Yet the central shadow hanging over these discussions is the declining belief that North Korea is interested in pursuing anything other than a weak, interim agreement under which the regime would continue to keep a substantial nuclear capability. It is possible that a Trump administration might be willing to approach China about such an option, but only in the context of some promise of a final settlement. In the absence of such a promise — and given that such an assurance is not credible — it is hard to imagine the United States going too far down the road of further concessions, including sanctions relief. Unless the highly unpredictable President Trump chooses to take a risk on direct bilateral negotiations, we are entering a period in which sanctions relief will be relegated to a long-term prospect and the pursuit of further constraints — both economic and military — will dominate the policy discussion in the United States.

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