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North Korea-Japan Relations: The Normalization Talks and the Compensation/Reparations Issue

Mark E. Manyin
Analyst in Asian Affairs
Foreign Affairs, Defense, and Trade Division

Summary

Japan and North Korea have not established official relations since North Korea was founded in 1948. In 2000, the two countries held three rounds of normalization talks, which had been frozen since 1992. The talks, however, have been stalled since November 2000. One of Pyongyang's key demands is that Tokyo compensate North Korea for Japan's colonization of the Korean Peninsula from 1910-1945. Though Japan has resisted using terms such as "compensation" and "reparations," Tokyo has offered to provide North Korea with a large-scale economic aid package, much as it gave South Korea economic assistance when Tokyo and Seoul normalized relations in 1965. North Korea, however, insists that it will only accept "compensation." This disagreement over terminology has contributed to the current deadlock in the normalization negotiations.

The 1965 Japan-South Korean settlement consisted of a \$300 million grant, \$200 million in low-interest long-term government loans, and \$300 million in private credits from Japanese financial institutions. There are a number of estimates for the present value of the 1965 Japan-South Korea settlement, ranging from as low as \$3.4 billion to over \$20 billion. One methodology that adjusts for inflation in Japan and for inter-Korean population differences yields a 1999 value of approximately \$3.8 billion. Reportedly, Japanese officials are discussing a package on the order of \$5-\$10 billion.

This report will be updated periodically to track developments in the Japan-North Korea normalization talks.

Background

In the fall of 1999, William Perry, Special Advisor to the President on North Korea, unveiled a new strategy for halting North Korea's nuclear weapons and long-range missile

programs.¹ One of the “carrots” in the United States’ policy appears to be a prospective large-scale economic assistance package, conditional upon North Korea’s cooperation.² It is widely believed that one of the largest source of economic aid to Pyongyang would come from a prospective Japanese offer of monetary “compensation” for its colonization of the Korean peninsula in the first half of the 20th Century.³ To this end, South Korea and the Clinton Administration – the former under its so-called “sunshine policy” toward North Korea – urged Japan to reduce tensions with North Korea.⁴ Tokyo and Pyongyang have not established official relations since North Korea was founded in 1948. North Korea insists that before it will establish relations with Tokyo, Japan must provide an apology and monetary compensation to resolve Japan’s past treatment of Korea.⁵ Japan has agreed in principle to offer an economic package to North Korea, but has been vague about its amount, form, timing, and characterization.

In 2000, North Korea improved relations with all the major countries in Northeast Asia, with the exception of Japan. Most dramatically, South Korean President Kim Dae Jung and North Korean leader Kim Jong-il held the first-ever inter-Korean summit meeting in mid-June. The two leaders pledged to take steps toward an eventual reunification, including setting up economic cooperation projects between the two Koreas. Two weeks before the summit, Kim Jong-il traveled to Beijing, his first trip to China since the death of his father and predecessor, Kim Il-Sung, in 1994. Shortly after the summit, the U.S. lifted most of its remaining economic sanctions on North Korea. In July 2000, Russian President Vladimir Putin visited North Korea, signaling a thaw in Moscow-Pyongyang relations, which have been icy since the Soviet Union established relations with South Korea in 1990. These diplomatic moves by North Korea have placed even greater pressures on Tokyo to improve relations with Pyongyang.

The Japan-North Korea Normalization Talks - Issues and Chronology

Disagreements over the Economic Settlement Package. Regarding the size of Japan’s economic package to North Korea, official figures have not been released by either side, though Pyongyang reportedly has demanded \$10 billion at minimum. Some Japanese experts believe that North Korea will ask for a settlement in the \$20 billion range. According to Japanese North Korea-watchers, no consensus has been reached in Tokyo

¹ See William J. Perry, “Review of United States Policy Toward North Korea,” Unclassified Report, October 12, 1999, available at [http://www.state.gov/www/regions/eap/991012_northkorea_rpt.html].

² “Japan’s Approach to DPRK Viewed,” *SISA Journal*, November 18, 1999, translated by the Foreign Broadcast Information Service, FTS19991128000519.

³ Marcus Noland, “The Economics of Korean Unification,” prepared for *Foresight Magazine*, February 2000, available at [<http://www.iie.com/TESTMONY/foresigh.htm>]. Victor Cha, “DPRK Dialogue,” *Comparative Connections*, 4th Quarter 1999, [<http://www.csis.org/pacfor/cc>].

⁴ “Seoul Urges Tokyo to Compensate Pyongyang for Colonial Rule,” *Korea Herald*, May 7, 1999. For a detailed discussion of South Korea’s sunshine policy, see Rinn-Sup Shinn, *South Korea: “Sunshine Policy” and its Political Context*, CRS Report RL30188.

⁵ See, for example, “Text of North Korean Government Statement Against Japan,” *BBC*, August 13, 1999.

on Japan's bottom line, though there have been reports that Japanese officials are discussing a package on the order of \$5-\$10 billion. According to one report in the Japanese press, Japanese officials in October 2000 were considering a \$9 billion package.⁶ Observers suggest that Tokyo will argue that \$2 billion be deducted from the final amount in order to give Japan credit for its \$1 billion contribution to the Korean Peninsula Energy Development Organization (KEDO) and the \$1 billion North Korea owes Japanese sources (mainly Japanese banks) from unpaid debts incurred in the 1970s and 1980s.⁷

In addition to the size of the settlement, the two sides have clashed over terminology. Japan is refusing North Korea's demand that the package be labeled as "reparations," or even "compensation." Instead, Tokyo has offered to characterize the monies as "economic assistance," as it did in the 1965 Japan-South Korean normalization negotiations.⁸ This semantic dispute has momentarily stalled the talks. Other issues likely to be contentious include the conditions placed on Pyongyang's use of the aid/reparations, and the composition of the money – grants or loans.⁹ Additionally, North Korea is demanding that Japan issue a formal, "legally binding apology" from the Japanese emperor and/or prime minister. Japan has countered that a sufficient apology was extended as part of 1995 statement by then-Prime Minister Tomiichi Murayama expressing regret for Japan's past actions.

Other Contentious Issues. Any normalization agreement will be politically difficult for the Japanese government. In recent years, relations with North Korea have become a high-profile political issue in Japan, due to North Korea's 1998 Taepodong missile launch over Japan, its 1999 naval incursion into Japanese waters, and the release of new (albeit unconfirmed) evidence that Pyongyang kidnapped Japanese citizens in the 1970s and 1980s.¹⁰ Public opinion polls indicate that most Japanese favor adopting a cautious approach toward North Korea.¹¹ Conservative groups in Japan – including many members of the dominant Liberal Democratic Party – opposed the government's decisions in March and October 2000 to resume shipments of food aid to North Korea, arguing that Japanese assistance should be conditioned on Pyongyang's cooperation on the abduction cases and on missile and nuclear weapons issues.¹² An additional concern expressed by

⁶ Tokyo Shimbun, October 26, 2000.

⁷ Author's conversations with Japanese North Korea experts following CRS Workshop, "Dealing with North Korea," March 2, 2000; see also Cha, "DPRK Dialogue."

⁸ "Kono Confirms Offering Economic Cooperation to N. Korea," *Kyodo*, August 25, 2000. Japan's position is that since it has never been at war with North Korea, it is not required to pay reparations.

⁹ Cha, "DPRK Dialogue."

¹⁰ For more on how the North Korea threat has caused many Japanese policymakers to rethink Japan's defense posture, see Richard Cronin, *Japan's Changing Security Outlook*, CRS Report RL30256, July 9, 1999. See also Rinn-Sup Shinn, *North Korea: A Chronology of Provocations, 1950-2000*, March 15, 2000.

¹¹ According to a 2000 poll, only 36% of Japanese surveyed believed Japan should resume food aid to North Korea, compared with 51% in August 1997. *Mainichi Shimbun*, February 27, 2000.

¹² On March 7, 2000, Japan announced its intention to deliver 100,000 tons of rice to North Korea, (continued...)

these groups is that Japanese compensation or food aid might be used for North Korea's military rather than for its populace. During the April 2000 talks, the Japanese delegation also raised the issues of North Korea's alleged drug-trafficking, and its alleged biological and chemical weapons programs.

The 9th Round (April 2000). In the April 2000 Japan-North Korea talks, North Korea insisted that relations be normalized only after completing a "settlement of the past," a phrase Pyongyang defines to include four items: an apology, compensation, the return of cultural assets taken from Korea during the occupation, and the granting of legal status to ethnic Koreans living in Japan. For future negotiating rounds, North Korea proposed establishing panels to deal with other outstanding issues, including Pyongyang's missile development program and the whereabouts of ten Japanese allegedly kidnapped by North Korean agents. Japan, seeking to avoid decoupling the compensation/apology issue from the kidnaping and missile disputes, rejected the North Korean proposal.

The 10th Round (August 2000). On July 26, 2000, the Japanese and North Korean Foreign Minister staged an unprecedented meeting at the ASEAN Regional Forum meeting in Bangkok. The two officials agreed to hold another round of talks in Tokyo in August. They also agreed to resume discussions over further visitations to Japan by women who married Korean husbands and emigrated to North Korea.

At the August 21-24, 2000 bilateral meetings in Japan for the first time formally raised the possibility of providing an economic assistance package – *i.e.* not a compensation payment – to North Korea. Reportedly, no figures were discussed, and North Korea did not respond to the offer. The two sides agreed to hold another round of talks in a third country in October, with a goal of establishing diplomatic ties by the end of 2000. The negotiators also agreed to expand bilateral contacts to include politicians and business enterprises, and to set up committees to handle two of North Korea's demands: the return of cultural treasures taken from Korea during the Japanese occupation, and improving the legal status of Koreans living in Japan. Reportedly, North Korea asked Japan to resume trade insurance and full-scale economic aid, but Japanese negotiators declined.

The 11th Round (October 2000). Almost no progress was achieved during the October 30-November 1, 2000 bilateral meetings in Beijing. Reportedly, North Korea flatly rejected Japan's proposal to offer economic assistance in lieu of compensation. Japan again turned down North Korea's demand that the abduction issue be discussed outside the normalization talks. A sign of the deadlock is that the two sides did not set a date for the next round of talks.

Japan's 1965 Economic Aid Package to South Korea

On June 22, 1965, Japan and South Korea signed a Treaty of Basic Relations, normalizing relations between the two countries for the first time since Japan annexed the

¹² (...continued)

its first shipment since the food aid program was suspended following Pyongyang's launch of a two-stage Taepodong missile over Japan in August 1998. In October 2000, Japan announced it would send an additional 500,000 tons of rice aid to North Korea.

Korean peninsula in 1910. As part of the final settlement, Japan agreed to provide South Korea with a total sum of \$800 million¹³, which consisted of: a) an outright grant of \$300 million, to be distributed over a 10-year period; b) a \$200 million loan to be distributed over a 10-year period and repaid over 20 years at 3.5% interest; c) \$300 million in private credits over 10 years from Japanese banks and financial institutions.

Prior to the 1965 agreement, the normalization negotiations between Tokyo and Seoul had dragged on for over fourteen years, and had triggered strong emotions in both countries. Throughout the 1950s, South Korean President Syngman Rhee adopted a confrontational approach toward Japan, and successive Japanese governments showed little enthusiasm for accepting Rhee's demands that Japan apologize and compensate for its colonization of the Korean peninsula.

Relations warmed dramatically following a military coup in 1961, led by general Park Chung-Hee, who established rapid industrialization – following the Japanese model of export-led development – as his country's paramount economic goal. To this end, Park was eager for Japanese economic assistance, and adopted conciliatory postures on most outstanding issues. The approximate size and composition of the compensation package was one of the first issues to be resolved following Park's coup. The South Korean side, which at one point had asked for as much as \$2 billion, lowered its demands to \$700 million in grant aid before agreeing to the \$800 million total package. Reportedly, until late 1962, Japan had offered only \$70 million in total compensation, a figure the U.S. State Department at the time described as “unrealistically low.”¹⁴ Furthermore, the Treaty on Basic Relations did not contain any reference to a Japanese apology. Instead, Japan's reparations payment was characterized as “economic assistance.”

The terms of the Treaty enraged many South Koreans. Charging that the agreement amounted to a “sellout,” Korea's opposition parties boycotted the ratification process in the National Assembly. Violent anti-government protests erupted throughout the country, and the Park government imposed martial law to suppress anti-government protests around the country, the second time in less than a year troops were mobilized to curtail protests against the government's Japan policy. The agreement also faced strong but eventually ineffectual opposition in Japan, where the Socialist Party – which had friendly ties with North Korea – argued that the Treaty would impede Korean unification and was a prelude to an anti-communist alliance in Asia.¹⁵

Estimating the Present Value of the 1965 Settlement

There are a wide range of estimates for the present value of the 1965 Japan-South Korea settlement. At the low end is a method that adjusts for inflation in the U.S.

¹³ According to the South Korean Ministry of Foreign Affairs and Trade, the aid was distributed in dollars, not yen.

¹⁴ *Foreign Relations of the United States, 1961-1963, Volume XXII (Northeast Asia)*, 567-69; Chong-Sik Lee, *Japan and Korea: The Political Dimension* (Stanford, CA: Hoover Institution Press, 1985), 50.

¹⁵ Lee, *Japan and Korea*, 55.

economy, yielding a value of approximately \$3.4 billion in 1999 dollars.¹⁶ At the high end is a calculation that produces a value of \$20 billion in today's dollars by adjusting for inflation in the Japanese economy, appreciation of the yen, accrued interest, and differences in population in North and South Korea.¹⁷ One methodology that adjusts for Japanese inflation since 1965 and for inter-Korean population differences yields a present value of ¥418 billion (\$3.8 billion using an exchange rate of ¥110 = \$1). If the same disbursement formula used in 1965 were applied today, the ¥418 billion would break out as ¥157 billion (\$1.42 billion) in outright grants, ¥104 billion (\$950 million) in concessionary government loans, and ¥157 billion (\$1.42 billion) in private credits.¹⁸

The above figures should be interpreted as rough approximations. Computing the present value of a past sum is an inherently inexact task. When more than one country is involved, the calculation is made even less precise by long-term changes and short-term fluctuations in exchange rates. Additionally, an exact calculation would take into account differences between North Korea and South Korea, including the extent of the claims for damage by the Japanese occupation. Finally, the adjustments are made for the total figure of \$800 million, even though the actual value of Japan's compensation package was lower: Over 60% (\$500 million) of the settlement was disbursed as government loans and private credits, which are less valuable to the recipient than outright grants. Thus, the calculations presented, although providing a preliminary comparative baseline, tend to overstate the present value of Japan's settlement with South Korea.

On the other hand, the 1965 settlement occurred before the revelation that Japan had forcibly used tens of thousands of Korean "comfort women" to provide sexual services to Japanese soldiers during World War II. North Korea is insisting that Japan's compensation take into account the comfort women's plight, a demand that (if it is met) presumably would raise the value of the settlement package.¹⁹

¹⁶ This method uses the U.S. gross domestic product (GDP) deflator to adjust for inflation between 1965 and 1999. The GDP deflator is the ratio of nominal GDP in a given year to real GDP in that same year. In 1999 the GDP deflator was 104.37 (1996 = 100), 4.35 times the 1965 deflator of 23.98. Thus, \$800 million in 1965 dollars would be worth approximately \$3.4 billion in 1999 dollars.

¹⁷ Noland, "The Economics of Korean Unification." For his accrued interest adjustment, Noland assumes an annual rate of return of 5%. Noland acknowledges that the Japanese side is likely to reject the notion of adjusting for accrued interest, on the grounds that North Korea's intransigence is to blame for the perennially stalemated normalization talks. March 2000 conversation between Marcus Noland and the author. According to the U.S. Census Bureau, in 1965, North Korea's population was approximately 11.9 million, approximately 40% the size of South Korea's population of 28.7 million in the same year. In 1999, North Korea's population was estimated to be 21.4 million, around 45% the South Korean total of 47 million.

¹⁸ This method uses the Japanese GDP deflator to adjust for inflation between 1965 and 1999. In 1999 the Japanese GDP deflator was approximately 3.5 times the size of the deflator in 1965. Using this figure, the 1965 compensation package of ¥288 billion would be worth roughly ¥1.01 trillion today (\$9.2 billion, at ¥110 = \$1). To adjust for population differences, multiply ¥1.01 trillion by 0.41, which is the ratio of North Korea's 1965 population (11.9 million) to South Korea's 1965 population (28.7 million). The result is ¥418 billion (\$3.8 billion).

¹⁹ *Yomiuri Shimbun*, April 8, 2000.