**North Korea’s Pegged Won Wiggles, But Doesn’t Break, Yet[[1]](#endnote-1)**

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North Korea’s won has slipped ever so slightly against the dollar in recent weeks, not surprising given the dollar’s worldwide strength, but presenting an interesting conundrum for the Chosen central bank. It no doubt knows that pegged currencies can break suddenly when a small divergence, a wiggle, catches the public’s attention, which sensing the authorities are running out of reserves, dumps the local money in a panic exchange for safer assets. A self-sustaining downward spiral can occur, eviscerating the currency and causing all kinds of social instability.

This began to happen in North Korea in 2009, when money was much less important, and stopped only with Kim Jong Un’s father’s execution of the party finance chief and a very rare Worker’s Party apology. Likely learning a big lesson, under Kim, the financial authorities have done an extraordinary job keeping the won stable, even with extremely tough sanctions against it, and have done so by allowing free circulation of competing assets, the US dollar and the Chinese yuan. And, likely, being very parsimonious in printing its own notes or extending credit, a tight money policy that no doubt squeezes the state’s economy. So, the question on every North Korean’s mind, and especially on Kim’s as he travels to Beijing, must be, how long can this last.

* North Korea Daily reports the dollar traded at 8,500 won in Pyongyang on 26 December, up from a steady 8,000 won through the middle of the year, a won devaluation of 6 percent.
* Against the globally weaker yuan, won has been more volatile, but without the trend decline. (graphs are roughly same scale)
* The cross rate implied by the won for dollars and yuan is now exactly consistent with the overseas dollar/yuan rate, after a significant divergence in mid-2018 probably gave room for arbitrageurs to speculate and make money. This suggests a remarkably free flowing foreign exchange market in North Korea, given its socialist underpinnings.

One is hesitant to guess what caused the recent dollar uptick, either market forces surrounding the strong dollar overseas or, more likely, the continuing drain on the country’s foreign exchange exhibited by the huge drop in its exports due to sanctions. Chinese merchandise trade data suggest a $200 million monthly outflow for most of 2018, unlikely offset by significant services or remittances inflows.[[2]](#endnote-2)

* Recent commodity-by-country trade data released by China, after a six-month delay, show an incredible absence of exports of electrical and non-electrical machinery, and vehicles to North Korea, suggesting the country is running out of foreign exchange and can’t afford any investment related purchases.

Another guess might be that the authorities are trying to inoculate the market so as not to expect a firm peg, so future movements will not be seen as policy failures or an impending crisis. If this is the case, we should see the dollar fall back to the 8,000 won level quickly as the central bank intervenes and spends dollars to buy back won. And yet another guess, expressed recently by some scholars, is that the won is actually more closely tied to yuan so that the yuan decline against the dollar automatically made for the won decline. As seen in the above graphs, however, the won value against the yuan has tended to be much more volatile than against the dollar. Alternatively, some kind of basket approach may be in use but that removes the confidence building features of a simple dollar peg, and confidence is what North Korean markets need more than anything.

What we do know is anyone holding dollar assets in North Korea over the past few weeks has become relatively better off than those holding dollar liabilities—apartment mortgages are said to be in dollars—or those loyal citizens who only hold won who are now relatively worse off. One might think this could be cause for regime concern. We don’t know but is it enough for a quick trip to Beijing and a friendly chat with President Trump?

1. The author is indebted to Daily North Korea which diligently reports North Korean prices and exchange rates in its newsletter. https://www.dailynk.com/ [↑](#endnote-ref-1)
2. Next week I will analyze this important release of detailed Chinese commodity trade with North Korea. [↑](#endnote-ref-2)