

# **International Trade and Economic Policy of Northeast Asia:**

## ***The Role and Interests of Russia***

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The goal of my presentation is twofold:

- to elaborate in what way Russia could constructively contribute to the ongoing regional integration processes in East Asia and Northeast Asia (NEA);
- to find out what models of regional integration would better suit Russian critical interest – to sustain underdeveloped and under populated territories of its Russian Far East (RFE).

During a long historic period (from 30s till 90s) great economic and financial resources and subsidies had been pouring by the Government into the Russian Far East that had been considered as a bastion a military power in the Pacific. However, at the beginning of the 90-s in last century most of the state orders for the local military industry had been cancelled, and all subsidies for the region in such spheres as transport, energy, wages, etc. had been stopped, and the socioeconomic situation in the RFE has changed radically to the negative. As a result of that the RFE has been transformed into a depressed territory, and during 15 years the region lost one and a half million in population (1990 – 8 mln. people, 2007 – 6,5 mln people).

In 2000 newly elected President Vladimir Putin demonstrated willingness to improve the situation. While addressing the Asia-Pacific and Russian Far East's audiences he declared that multilateral cooperation programs in energy, and transportation infrastructure development projects in Northeast Asia would have been most profitable for the countries of this region, and the best option for the RFE population to improve standards of living.

Most part of those proposals looked like a rhetoric for a while, but gradually some changes became to happen that reflected a new situation in the Russian economics operating in a new environment of the Russian state budget's huge surplus beefed up by oil dollars. In 2005 then Minister of Economic Development and Trade German Gref said that the Russian Government must and would take part in construction of roads, airports, pipelines, energy power grids, and

that the Government decided to increase the amount of money allocated to the RFE development programs: from 2,9 bln rubles<sup>1</sup> in 2004, to a sizable amount of 17,5 bln rubles in 2007.

However current world economic and financial crisis played a negative role - some regional development projects has been stopped or delayed.

Overall, the Asia Pacific region is an important component of the Russian foreign policy, because Moscow is interested to use its increasing economic potential to contribute to the economic development of the Russian Far East and Eastern Siberia. There are several areas of Russia's regional involvement that could become substantial components of the EA and NEA multilateral cooperation: energy and natural resources supplies; transportation services, nature and ecology preservation, science and education; constructive participation in regional and subregional International Governmental Organizations (IGO), etc.

### **Russian bilateral economic and trade ties with NEA countries and the U.S.**

Three NEA countries (China, Japan, and ROK) are the leading trade partners for Russia and her Far Eastern territories. On a country to country basis China is a clear leader: in 2008 her annual trade volume with Russia reached \$56 bln, while Japan and ROK were trailing behind with \$20 bln and 15 bln respectively. Considering the RFE, situation is more balanced. In 2007 the RFE territories annual trade output had been as follows: \$6.8 bln with Japan, \$5.8 bln with ROK, and \$4.9 bln with China. It is important to note that during last several years when first Sakhalin projects became operational, oil and oil products became main components of Japanese and Korean exports from the RFE.

**(For details see – Power Point slides)**

#### *China*

For a number of security and economic reasons, Russia's policy in Asia gives priority to its partnership with China. In 2004 Russian President Putin made a historic visit to China that led to final demarcation of the 4,300-kilimeter long Russian-Chinese border. Moscow and Beijing have become partners in strengthening stability in adjacent regions, such as Central Asia (the Shanghai Cooperation Organization) and NEA (Six-party talks). Beijing is gradually increasing its role in multilateral security and economic cooperation by making such contributions as

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<sup>1</sup> One US dollar is equivalent to 32-33 Russian rubles

proposing to invest 10 billion US dollars to stimulate trade and economic cooperation between SCO member-states, and by arranging Beijing to be a constant negotiation venue for Six-party talks as well as a headquarters for the Greater Tumen Initiative.<sup>2</sup>

Russian–Chinese trade was rapidly increasing: in 2008 it has reached a record \$56 billion. One of the main trade boosters is an expansion of its border trade component.

As far as the Chinese illegal migration threat is concerned, Moscow and the regional political elites are sure that Russia needs a foreign labor force to develop vast territorial spaces in the RFE and East Siberia. The issue is how to construct adequate laws and then implement an effective immigration policy. In the RFE, more than 70% of legal working migrants are from China. Their total number is around 30 thousand people (10-12 thousand people work on a contract basis in agriculture, construction, etc.; 12-15 thousand are traders; plus several thousands are students and businessmen). Other sizable migrants groups are from North Korea and Vietnam.

### *Japan*

During last 15 years the Russian-Japanese relationship has been characterized by obvious contradictions. On the one hand, the geopolitical interests of both countries depend on radical improvements in bilateral relations. On the other hand, Moscow's proposal for joint economic development of the southern Kurile Islands, without the transfer of sovereignty to Japan, did not get a positive reply from Tokyo. At the moment both sides are not ready to soften their position on the issue. Overall, bilateral relationship has been composed of two unequal elements: a slowly widening network of cooperation in various fields and long-term territorial dispute over the southern Kurile Islands.

Mutual trade turnover between the two countries increased from the decent level of \$5 billion in 2003 to a record \$20 billion in 2007. Japanese companies invested a lot of money into Sakhalin oil and gas extraction, processing and transportation projects. Besides, Russia is really interested to attract Japanese investments into other (not natural resources development) industry sectors, and that was why Moscow was very encouraged by Nissan and Toyota decisions to build automobile producing plants in Russia.

### *The Korean Peninsula*

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<sup>2</sup> Sevastyanov S. The Russian Far East's Security Perspective: Interplay of Internal and External Challenges and Opportunities. In eds. by A. Iwashita Siberia and the Russian Far East in the 21<sup>st</sup> Century: Partners in the "Community of Asia". – Sapporo: Slavic Research Center, 2005. P.27.

Russia is trying to maintain balanced political ties with ROK and DPRK, and to fully participate in solving economic and security problems on the peninsula. In the economic area South Korea overwhelmingly dominates: in 2007 Russian trade with RK reached a record level \$15 bln, while Russia – North Korea annual trade in 2007 was only \$120 million. All three countries (RF, ROK, DPRK) consider implementation of joint projects in energy and transportation as major factors in decreasing tension on the Peninsula and eventually in securing unification of Korean states.

Trans-Siberian Railroad (TSR) extension to the Korean Peninsula and its connection to the Trans-Korean Railroads (TKR) is considered as most perspective and profitable international transportation project. Joint use of TSR and TKR would help ROK and Japanese business to decrease cargo transportation period to European countries three times (from 30-35 days by sea to 10-12 days by land), while Russia and DPRK would get much more profit for the transit of increased amount of containers.

Characterizing Russian energy export to NEA countries, one regional security problem should be taken into account. Most of Russian proposals to sell oil, gas and electricity to its neighbors could not fully materialize until Korean Peninsula security issue is solved. To make this happen, Russia is actively participating in 6-Party Talks. Moscow believes that a solution to this problem would be facilitated by providing DPRK with adequate guarantees of security and by creating conditions for its sound economic and social development in exchange for renunciation of its military nuclear program.

#### *The United States*

Though Moscow and Washington successfully cooperate in 6-Party Talks, the potential for closer ties between the RFE and USA is underexploited especially in economics sphere: bilateral trade and investments substantially declined in this century. The only positive examples in economics sphere are Sakhalin-1 project with an active Exxon participation, and latest investments into mineral extraction projects in Yakutiya.

#### **The Russian Far East's New Economic Development Plans and Initiatives**

An idea to form multilateral framework for cooperation in the energy sector in NEA had been gaining momentum in the region for more than 15 years. However in reality in 2004 the Russia started construction of the Eastern Siberia - Pacific Ocean (ESPO) oil pipeline *using state budget money and not seeking any foreign investments to start this project.*

The ESPO first section from Taishet, Irkutskaya oblast to Skovorodino, Amurskaya oblast should be able to support a total delivery capacity of 80 mln tons of oil per year. Two other proposed pipeline portions starting in Skovorodino (the main one - going to Primorsky region, and an off-shoot - to Datsin, Northern China) should have an annual capacity of 50 mln tons, and 30 mln tons respectively. In 2009 Russia signed an epochal agreement with China. In accordance with this document during next 20 years Russia would deliver to China 300 million tons of oil, and for this oil China would pay more than \$100 bln. For Moscow this is a principal decision, and it means that at this point in time an off-shoot to Datsin became politically and economically more important than a main route to Primorsky region.

Another attractive option for energy cooperation in NEA is hydropower. In 2006 inexpensive energy produced at the Bureya hydropower station, Amurskaya oblast, has been brought via high voltage lines to Primorsky region that is bordering North Korean territory, thus offering Pyongyang a practical source of energy. It should also become a reliable source of affordable energy for China and ROK.

*Two public companies (Gazprom and Rosneft) are clear Kremlin favorites. In 2007 Putin signed a decree allowing Gazprom and Rosneft to get equal share of all Russian continental shelf to extract oil and gas. That decision blocks foreign and other Russian companies from getting major share in these projects, and leaving them with a role of not owners but contractors/subcontractors.*

*Both above mentioned companies have chosen Northeast Asia and the Russian Far East as areas of their expanded investments' activities.*

*Gazprom priority in the region is to sell Sakhalin area extracted gas to local consumers in the RFE and later to foreign partners. Gazprom recently bought a control share of the Sakhalin-2 project. Gazprom became an owner of the Sakhalin – Komsomolsk-at-Amur – Khabarovsk gas pipeline, and in 2009 this company started a new project to prolong this pipeline from Khabarovsk to Vladivostok thus bringing it near the border with China and DPRK. This Sakhalin – Vladivostok gas pipeline should become operational in 2011. This pipeline will first bring gas to the Russian Primorsky territory, and from 2014-2015 it would be ready to support neighboring countries using resources from the Sakhalin-3.*

Sakhalin-3 project has been chosen by Gazprom as a main resource base to support its plans to deliver gas by a pipeline to internal and foreign consumers in Northeast Asia. Sakhalin-3 is composed of four gas and oil fields with total resource base of more than 700 mln tons of oil and

1,3 bln cubic meters of gas (just for comparison, joint total resource base of Sakhalin-1 and Sakhalin-2 is about 450 mln tons of oil and 1,0 bln cubic meters of gas).

Besides, Gazprom and Korean Gas Company Kogas are considering a feasibility of constructing a gas pipeline from Kovikta gas field in Eastern Siberia to South Korea going through the Chinese territory.

*ROSNEFT also has an ambitious investments' program abroad and in Russia.*

ROSNEFT is developing strategic partnership with Chinese National Petroleum Company (CNPC) – one of the largest oil companies in the world delivering the lion's share of oil and gas to China. Rosneft and CNPC plan to form a joint venture to make geological survey in Eastern Siberia prospecting for oil reserves at the new areas. In partnership with the CNPC, Rosneft also plans to construct in China an oil processing plant and about 300 gasoline stations. The Chinese public energy companies, until recently, focused on Siberian energy projects, but they decided to participate in the Sakhalin offshore ventures.

“Program of the gas industry development in the Eastern Siberia and the Russian Far East” has been approved by the Russian Ministry of Industry and Energy in 2007. The total amount of investments to realize this program will be 2,4 trillion rubles (about \$93 bln). In accordance with the program coordinated by Gazprom, by the year 2020 (in comparison with 2006) the volume of gas extraction will increase 18 times. In material terms it means that delivery of gas to local consumers in eastern part of Russia will increase up to 27 bln cubic meters per year by 2020, and will reach 32 bln cubic meters per year by 2030.

The program clarifies that **gas extraction surplus** will be delivered to China, ROK, and other APR countries. By 2020 China and ROK annual import of gas from Russia will reach 25 - 30 bln cubic meters, and other APR countries will annually buy 20-21 bln cubic meters.<sup>3</sup>

### **Russian Approach to Multilateralism in the Asia-Pacific region**

*At the Asia Pacific level* Moscow is using APEC as a key international organization to promote its economic interests in the region. During last several years Moscow managed to make more visible input to the implementation of the APEC annual agenda selecting Vladivostok as a venue of such events as: 7<sup>th</sup> Investments Symposium in 2003; Meeting of the APEC Transportation

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<sup>3</sup> Lenta.ru, September 10, 2007

Working Group 2005; Meeting of the APEC Industrial Science and Technology Working Group 2007. As a next critical step in this direction Moscow has chosen Vladivostok as a venue of the APEC Summit in 2012. This Summit should be of help for the RFE, and Vladivostok to attract attention of Russian and foreign investors.

### ***Northeast Asia***

For the last 10 years the RFE was actively participating in a number of multilateral economic cooperation projects in NEA, including TRADP. However Moscow blocked most of the TRADP plans being concerned about potential loss of control over and ecological threats to strategically important part of the Primorsky territory, and about producing critical competition to local Russian ports.

The Tumen River Area Development program (TRADP) and its successor the Greater Tumen Initiative (GTI) so far is the only one example of the intergovernmental mechanism in NEA for economic cooperation. During its history of operation TRADP demonstrated several shortcomings and liabilities as follows:

1. Participating states interests and visions' controversies.
2. The project has never become participating states' priority. As a result leading international financial institutions (WB, EBRR, ADB) were not interested to support it.
3. TRADP incomplete regional membership: absence of Japan as a possible leading financial donor.

To increase operational effectiveness, in 2005 TRADP finally evolved into the GTI with an increased operational geographical area. A critical issue for GTI now is to enhance multilateral cooperation by putting its plans and activities into the context of the NEA larger political initiatives. At the same time GTI proposed plans should be effectively coordinated with participating states own priorities in developing this region.

### ***Special role for Vladivostok in NEA and GTI cooperation models***

In 2012 the APEC Summit will take place in Vladivostok, and to improve the host city's infrastructure the "Big Vladivostok" project is developed. The project capital will amount to about \$6 bln. It should be implemented during three years (2009-2011) on the basis of the public/private partnerships. The complex of "Big Vladivostok" project includes: reconstruction of the international airport, development of road network, including construction of two bridges (to Churkin Peninsula and to the Russian Island), development of port infrastructure,

construction of the multipurpose administrative business center, including large 4-5 “stars” hotels and international conference center for 7 thousand people.

Realization of this complex project would support the role of Vladivostok as a “key city” that by the quality of its infrastructure and services could be compared to such NEA cities as Dalian, Tianjin, Niigata, Sapporo, Busan, etc. Vladivostok is envisioned to become one of the NEA centers in providing such critical services as transportation and logistics; tourism; international education (after APEC Summit several hotels would be transformed into dormitories for Russian and foreign students of the new Federal university to be formed at the Russian Island. At this moment foreigners already complement a sizable amount of students’ body in several Vladivostok universities); scientific consulting in energy, environment and other spheres.

## **CONCLUSION:**

Negative demography and underdevelopment of vast territories are critical threats for the RFE and Eastern Siberia. To preserve the territorial integrity, Moscow is increasing public budget allocations to improve regional energy and transportation infrastructure thus indirectly improving local population standards of living due to positive collateral socioeconomic effects. To make proposed changes a reality the Russian Government should develop and undertake a more comprehensive long term program aimed at increasing attractiveness of the RFE to foreign capitals and Russian private investors, and to complement the above mentioned measures with one more critical component – to give the FRE territories more economic freedoms to start several free economic zones, tourist/recreational zones, etc.

From the mid 1990s Russian politics in the Asia-Pacific became more dynamic. Moscow became a full member of all critical trans-regional (APR) and subregional (NEA) INGOs, and it is important to continue active work in these formats. Recent decisions of the Russian leadership to host APEC summit in Vladivostok in 2012 and to take substantial financial and other obligations to help DPRK demonstrate that economic component of Russian regionalism in NEA is gradually reducing the gap with long time prevailing strategic balance of power and regional security agenda. In future Moscow should widen economic cooperation (with an emphasis on multilateral infrastructure development projects as clear symbols of regionalism) with NEA countries, and try to form more balanced relations with leading East Asian states and the U.S.

There are several promising areas of Russian cooperation with its foreign partners that could contribute to its integration into Northeast Asia.



First, the most perspective among them is to position itself as a major energy supplier to the East Asian countries. The fact that public companies Gazprom and Rosneft got a preferential access to the Russian natural resources may lead to slowdown in extraction ratio. At the same time in unfavorable climate and infrastructure conditions of the REF territories, oil and gas extraction and transportation could be effectively realized by public companies, such as Gazprom, Rosneft, Transneft, etc. They would be able to support stable supply of energy to Asian markets according to approved schedule and in quantities coordinated with foreign partners. Overall, Russia as a consolidated player at the Asian energy market could be a reliable partner to its neighboring countries. However, the latest efforts to restrict the participation of several of the largest foreign investors such as Shell and British Petroleum may reduce the number of foreign investors, especially private firms from developed countries, while increasing the presence of resource extracting companies from developing states such as China and India.<sup>4</sup>

China is the only country in Northeast Asia that could become a preferential “state-business” partner for Moscow. Such a partnership has already developed a firm intergovernmental basis (the Russo-Chinese strategic partnership),<sup>5</sup> as well as a business foundation (through a series of bilateral cooperation agreements between Gazprom and Rosneft from the Russian side, and CNPC, Sinopec, and other companies from the Chinese side). In recent years, Beijing has initiated a series of proactive investment activities in eastern Siberia and the RFE. However, the critical problem for Moscow is that China is seeking a substantial discount on the price of Russian resources. To avoid placing Beijing in the position of enjoying a buyer’s monopoly in price negotiations, Moscow should find ways to deliver a substantial part of its energy resources to Japan, the ROK and other countries. That is why, considering a proposal to form an International Governmental Organization for cooperation in energy sector in Northeast Asia, Moscow is still interested in its realization.

Second, Russia became a critical supporter of natural resources (timber, fish, seafoods, metals, etc.) to NEA countries. In future, Moscow should develop regional cooperation in natural resources preservation sphere, because all East Asian countries, especially China and Japan, are dependant on Russian energy, metals, timber, fish, and will depend even more in future.

Another area of possible Russian input - providing railway transportation services between East Asia and Europe by connecting TSR and TKR - could not be realized due to a nuclear problem at

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<sup>4</sup> Sevastyanov S. The More Assertive and Pragmatic New Energy Policy in Putin’s Russia: Security Implications for Northeast Asia // East Asia #25, 2008. PP. 35-55.

<sup>5</sup> Russia and China signed the Treaty on Good Neighborly Friendship and Cooperation on July 16, 2001

the Korean Peninsula. Moscow believes that everything possible should be done to solve it, and its role at the 6-Party Talks negotiation table may increase in future.

Finally, Russia's role as a consistent supporter of multilateral cooperation in the Asia-Pacific, primarily in security and economic matters, is gradually emerges. Multilateralism will be an important addition to the bilateral approach at all levels of the regionalism in the Asia-Pacific. For example, a multilateral solution to the Korean Peninsula security problem in a 6-Party Talks format may become a key to forming a new international governmental organization dealing with the NEA comprehensive security issues.

To increase NEA states' priority in implementing GTI Strategic Action Plan 2006-2015, its activities should be considered in the strategic context of the NEA political situation, and to be effectively coordinated with participating states own priorities in developing this region. In this case Russia would be more willing to increase its share in realization of those projects.