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THE RUSSIAN FAR EAST AND CHINA: THOUGHTS ON CROSS-BORDER INTEGRATION

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Introduction

“The Far East and Baikal are a strategic bridgehead of Russia, ensuring her military-political and economic influence in the Asia-Pacific region. The federal government and regions of the Russian Federation should jointly make huge efforts to give this region the dynamism that will permit it to be an effective and worthy region of Russia....” Viktor Ishayev, then-governor of Khabarovsk Krai, May 2003¹

Developing Russia's economically- and demographically-challenged Far East (RFE) has been a top priority for Moscow in recent years, consuming a significant and increasing share of state resources. Yet Moscow expects that much of the impetus for growth of this depressed region to come, not from within, but from closer integration with the relatively fast-paced economies of the Asia-Pacific region. For a variety of reasons – geographical proximity, economic imperatives, and close-fitting strategic ties – Moscow has assigned China a central role in its modernizing strategy, hoping to “catch the wind from China's rise in the sail of our economy,” as Vladimir Putin put it recently.²

Policy decisions in Moscow and Beijing have linked the development of the RFE and the adjoining Transbaikal region to the rejuvenation of the decrepit Soviet-built industrial base in northeast China – decisions that seemingly subordinate the economic future of the RFE to the requirements of China's industrial planners. Moscow evidently believes that closer integration with China will advance its geopolitical as well as its economic objectives in the East, which include establishing its credentials as a credible Asia-Pacific power. Yet this strategy could yield in opposite result. As integration with China proceeds apace, the RFE and Transbaikal over time may become more a part of Asia's periphery than Russia's periphery, and Russia could lose a measure of real sovereignty over these regions.

This paper will briefly address three main questions. First, how far has cross-border integration progressed between

¹ Cited in Dr Mark A. Smith “The Russian Far East: Drift from the Centre?” Conflict Studies Research Centre, September 2003, p. 3.

² “Cold Climate”, *The Economist*, August 31, 2013.

Russia's Far East territory and China? Second, what appear to be likely future trends in integration? Third, what policy issues do deepening Sino-Russian economic ties in the East present for Western countries and for the United States in particular? Three dimensions of integration will be emphasized: the RFE's foreign trade patterns, China's investment in the RFE, and land use by Chinese nationals in the RFE's border provinces.

TRADE

The RFE's foreign trade turnover as a whole is not excessively weighted toward China. Its three major partners – China, South Korea, and Japan – have had roughly equivalent shares, hovering close to 25 percent over the years observed (2011 through the first half of 2013). At the same time, different provinces exhibit vastly different degrees of trade dependence on the PRC, ranging from nine percent in Magadan to 99 percent in the Jewish Autonomous Oblast (JAO). Unsurprisingly, China accounts for the dominant share of trade with the four provinces that adjoin the Sino-Soviet border (Amur, JAO, Khabarovsk, and Primorye). On the other hand, the five Northern provinces (Chukotka, Kamchatka, Magadan, Sakha-Yakutia, and Sakhalin), which are relatively distant from China, boast a geographical variety of top-ranking partners: South Korea, United States, the United Kingdom, and (of all places) Belgium. (Different percentages associated with the RFE's foreign trade patterns are shown in Table 1.)

Table 1: RFE Provinces: Trade with China and Others

	Trade with China as Percent of Total Trade (2012)	Principal Trade Partners Percent (2012)	Trade with China as a Percent of GRP (2011)
Amur	90	China (90)	8.5
Chukotka	20	USA (33)	1.7
JAO	99	China (99)	5.0
Kamchatka	33	ROK (42)	6.8
Khabarovsk	43	China (43)	4.9
Magadan	9	UK (24)	1.5
Primorye	50	China (50)	23.0
Sakha-Yakutia	13	Belgium (46)	2.7
Sakhalin	13	ROK (41)	9.4
All RFE	28	ROK (28)	10.3

SOURCE: *Goskomstat: Regions of Russia*, various years

Trade dependency also can be analyzed as a ratio of a province's foreign trade to its Gross Regional Product (GRP). Here a somewhat different (and partially misleading) pattern emerges. As one might expect, commercial ties with China are essentially irrelevant to the economies of Chukotka, Magadan, and Sakha-Yakutia, but vitally important

to those of Primorye and Khabarovsk – provinces that together account for more than half the RFE’s population. (See Table 1) The relatively high dependence figure for Sakhalin – even though China is far from being its principal trade partner – is attributable to the fact that foreign trade accounts for 90 percent of that province’s entire economy, thus highlighting the significance of China’s share. On the other hand, the ratios for the JAO and Amur seem unrealistically low, given China’s dominant trade position in these provinces. One possible explanation relates to the so-called “suitcase trade” – a form of “legal” smuggling in which individual Russians (sometimes organized in gangs) travel to China, multiple times, carrying back goods purchased there, literally in suitcases, and declaring the merchandise as personal effects. Because customs statistics don’t adequately capture the extent of this “gray market” activity, the actual value of cross-border trade may be substantially higher than the official recorded value, as much as two to three times higher, according to one careful estimate.³

Furthermore, recent improvements or planned improvements in trans-border infrastructure will likely accelerate the growth of RFE-China trade. Last year, for example, a new pontoon bridge linking the Amur capital city of Blagoveshchensk and the neighboring Heilongjiang city of Heihe was put into operation (the cities face each other across an 800 meter stretch of the Amur River). Earlier this year, Russian authorities decided to reopen the Makhhalino Railway border crossing in Primorye, which will facilitate freight traffic between China’s Jilin province and the southern Primorye ports of Zarubino and Poset. A similar expansion of commerce can be expected from a planned (2014) construction of a new railway bridge, again across the Amur, which will connect the JAO town of Nizhneleninskoye with Tongjiang in Heilongjiang. Such developments will further cement relations across the border, strengthening the underpinnings of the Sino-Russian strategic partnership generally.

INVESTMENT

Though a serious trading partner for the RFE, China is not yet a serious investor in the region. Indeed, from an investment standpoint, Asia-Pacific integration has barely begun. According to Russia’s Interregional Association of Far East and Zabaikalye (a repository of official data for the regions) about two-thirds of the \$24 billion investment in the RFE Transbaikal (98 percent of which went to the RFE) in the two years 2011-2012, originated from a handful of Eurozone countries. Nearly all of that was channeled to mineral exploitation projects in two provinces: Sakhalin (oil and gas) and Sakha-Yakutia (diamonds and gold). Asian countries (mostly Japan and India) accounted for just 13 percent (\$3 billion), and China’s share (\$288 million) came to just slightly more than one percent of the total. About \$4 billion of investment were attributed to two tax haven countries, Cyprus and the Bahamas; this could increase the Asia-Pacific share somewhat, but the Cyprus portion reflects mostly Russian “round-tripping” (reinvestment at home from money stashed offshore) and the Bahamas-identified funds could have originated anywhere. In any event, whatever investment was routed through these jurisdictions does not alter the essential European character of this aspect of economic integration.

Of China’s \$288 million capital investment in the RFE Transbaikal, just \$107 million or a little more than one-third was dedicated to the RFE (most of the rest was directed to Zabaikalkrai Krai, possibly for mining projects there). Roughly three-quarters of the Chinese investment in the RFE flowed to the four border provinces – no surprise here – and among these, Primorye was the favored destination. See Table 2.

China’s weak investment footprint in the RFE reflects its conservative choices of projects – typically small-scale, low-risk, and quick-profit ventures in spheres such as wholesale and retail trade, services, low-level woodworking, and construction. China’s foreign economic strategy in the main, of course, is focused on acquiring resources vital to its industrial growth; yet China has generally been content to purchase the materials it needs rather than investing in the Russian companies that produce them. This strategy, though, could be changing. In early 2013 two metal concerns secured a 38 percent equity stake in a Russian iron ore company (IRC) with mines in Amur province for \$238 million – more than China’s entire investment in the RFE-Transbaikal in 2011-2012. And in October, a joint Russian-Chinese investment fund acquired a 42 percent share of the Khabarovsk-based Russian Forest Products Group, a leading forestry-holding company in the Russia’s Far East. Such ventures represent departures from the general pattern of Chinese business investment in the Far East, but could represent harbingers of deepening economic cooperation and trans-border relations generally.

³ Natalia Ryzhova “Peculiarities of Transmigrant Adaptation in the ‘Twin Cities’ of Blagoveshchensk and Heihe,” Blagoveshchensk, Amur State University, 2009, p. 9.

Table 2: Chinese Investments in the REF-Transbaikal by Province, 2011-2012, In Millions of Dollars

RFE	2011	2012
Amur	20.2	7.2
Chukotka	N/A	N/A
JAO	4.7	2.9
Kamchatka	1.0	2.0
Khabarovsk	1.5	2.5
Magadan	0.2	0.4
Primorye	31.5	14.8
Sakha-Yakutia	N/A	N/A
Sakhalin	8.4	1.5
Zabaikalye		
Buryatia	1.1	6.8
Zabaikalkrai	100.2	80.9
All RFE-Transbaikal	168.9	119.0

SOURCE: Interregional Association of Far East and Zabaikalye

A distinctively different kind of stimulus to cross-border integration will derive from projected Chinese (albeit Hong Kong Chinese) investments in Russia-based gaming operations. Projects announced and agreed on this year will focus on a newly-established gambling-hotel-entertainment zone in Primorski krai, near the Vladivostok airport. One group of investors, Hong Kong-listed casino operator NagaGroup, will spend \$350 million to build a casino resort complex in the zone featuring 100 gaming tables, 500 slots, 1,000 hotel rooms, as well as assorted bars and restaurants. A second group, comprised of Macao tycoon Lawrence Ho's Melco international and two Russian partners will invest \$630 million in a two-stage project to build its own complex in the zone; adding an additional 235 tables, 1,300 slots, and 720 hotel rooms to the overall total. These properties would represent a second Macao of sorts, taking advantage of Primorye's proximity to northeast China, and the putative gambling hunger of its millions of residents. The governor of Primorye Vladimir Mikliuchevsky ecstatically predicts that the new casinos will attract

four million tourists a year, further linking the economic fortunes of his province to the coat tails of its powerful and populous neighbor.⁴

LAND USE

Another significant measure of cross-border integration relates to Russia's policy of leasing vast tracts of land to Asian nationals, mainly Chinese, in the RFE's border provinces. With the state's blessing, Chinese agro-business and individual Chinese farmers engage in comprehensive land use schemes along the border, bringing in tens of thousands of Chinese laborers to actually work the land. Typically, property is leased on three to ten year contracts, and used to grow crops – soybeans, vegetables, grains, and fruits – for export back to China and/or sale within the internal RFE market. According to one frequently cited estimate, Chinese have leased some 426,000 hectares in Khabarovsk and the JAO, extensions encompassing nine percent of the JAO's arable land. A higher estimate puts the total at 850,000 hectares⁵ overall in the RFE. However, no reliable statistical information exists on the amount of land already rented to Chinese concerns. This is because the latter often employ subterfuges that circumvent local authorities and record-keeping (such as subleasing land unofficially from Russian lessees who "forget" to declare this kind of income on their tax returns). In other words, there is a spontaneous aspect to these land acquisitions, which raises disturbing questions about Russia's ability to control Chinese migration in border areas.

The economic rationale for this practice is rudimentary – an exchange of surplus land for surplus labor across contiguous territories. Russia also rents land to other Asian migrants, mostly Korean and Japanese, but the primary exchange linkage is with northeast China. On the Russian side, post-Soviet economic traumas – vastly reduced financial support for agriculture, combined with massive out-migration from the RFE (more than 20 percent since 1989, and almost 10 percent since 2000) – have idled millions of hectares of the RFE's potentially productive land. On the Chinese side, high population density, environmental degradations, urbanization, and shortages of water have seriously constricted opportunities in agriculture, pressuring many rural dwellers to set their sights on land north of the border.

The labor force the Chinese migrants provide has helped to sustain agricultural production in the RFE at a critical time in its history. Chinese farmers are said to obtain higher-than-average yields from their plots (though they are sometimes accused of using toxic chemicals that deplete the soil.) That's the economic good news. The political downside is that migrants could eventually acquire a permanent foothold in the RFE, seek preferential rights from Russian administrators of the borderlands, and even lobby for a special relationship of some kind with the provinces of their Chinese homeland (a *reconquista* scenario familiar to observers of US-Mexican border dynamics). Moscow seems partly aware of these risks; for example Prime Minister Medvedev warned last year without mentioning China specifically that "the objective of defending our Far Eastern territory from an excessive expansion of citizens from neighboring countries remains" and also urged avoiding "negative manifestations" such as creation of "foreign citizen enclaves."⁶ Yet Russian officials are dangling the prospect of leasing millions more hectares of RFE cropland to Asian agribusiness interests, so economic considerations remain paramount.⁷

POLICY ISSUES

Cross-border integration is official policy in Moscow and Beijing. China's industrial planning for its northeast has oriented its industries toward the processing of raw materials from the RFE and Transbaikal, while Russia evidently hopes that tapping Chinese capital, investment, and markets to develop its natural resource base will secure the future prosperity of these economically failing regions. The common policy of the partners was enshrined in a "Program of Cooperation" signed by then-Presidents Hu Jintao and Dmitri Medvedev in 2009 that explicitly linked the development of the RFE-Transbaikal to that of China's northeastern provinces.

The Program featured a list of 168 joint projects extending over all the RFE-Transbaikal provinces, and the 3 Manchurian projects (Heilongjiang, Jilin, and Liaoning). Those on the Russian side demonstrated a clear resource-

⁴ "Primorye Raskrutili," *Zolotoi Rog* (Vladivostok), September 17, 2013, p. 23.

⁵ Paul Goble, "Beijing Renting Foreign Border Area for Chinese Farmers," *Window on Eurasia*, June 1, 2010 and Andrew E. Kramer, "China's Hunger Fuels Exports in Remote Russia," *The New York Times*, June 9, 2010.

⁶ "Russia Fears Chinese Immigration Threatens Its Far East," *Agence France Presse*, August 10, 2012.

⁷ "Russia offers to lease land in the far east to APEC countries," *Russia and India Report* (Indus) January 30, 2012.

harvesting focus: mining, minerals development, forest harvesting, agriculture, water, power generation and transmission, and the like. By contrast, the Chinese projects mostly emphasized creation of a balanced and diversified manufacturing complex, aimed at producing a broad range of finished goods for end-customers. The Program also proposed improvements in infrastructure along the countries' mutual border, the better to facilitate the flow of Russian raw materials to northeast China's factories.⁸ To some Russian observers, this linkage scheme equated to putting some 45 percent of Russia's territory (the RFE plus Transbaikal) in the position of a resource colony or appendage to a metropolitan China. Moscow has acknowledged these concerns to some extent ("We are not entirely satisfied with the emerging trade structure" Putin told the Valdai Discussion Club in 2012)⁹ and Russian officials have pressed China to invest in higher value added or "deep processing" industries on Russian territory, but with little success so far.

Implementation of the Hu-Medvedev program has been slow; in fact, none of the 94 projects mentioned on the Russian side appear to have been completed to date though several were approved in 2010. But last October, the Ministry of Development of the Far East and China's State Development Bank signed a cooperation agreement under which the Bank would provide up to \$5 billion to finance projects within the scope of the Hu-Medvedev agreement and Russia's plan for development of the RFE-Transbaikal until 2025.¹⁰ The communique announcing the agreement emphasized infrastructure development – ports, roads, railways, bridges, and so forth – as well as "technologically- and environmentally-friendly" production, the latter probably a sop to Russian desires for more advanced-processing enterprises. But the underlying shape and rationale of the 2009 plan are not likely to change significantly; because China has no real interest in helping Russia move up the value added chain and because the RFE's integration with China under the current terms of trade is relatively well-entrenched.

The pro-China orientation of Russia's Far East development strategy is controversial and poses some risks to the Russian state. Moscow certainly is not planning to surrender its Far Eastern territories to China, but the balance of Moscow's decisions coupled with reality on the ground – the long common border and China's ascendant role in East Asia – all suggest that China's economic influence in the RFE-Transbaikal will grow significantly in years to come, potentially diluting Russia's sovereignty over these strategically vital regions. China's rivalry with the United States in the western Pacific will doubtless further this dynamic, as it seeks enlarged access to land-based raw materials to counter US maritime threats.

At the same time, Russia's democratic partners on the Pacific Rim and in the EU also have interests in the RFE, especially in its northern provinces, and are not anxious to see the resources and markets of that vital region drift irrevocably into China's economic orbit. The arguments presented in this paper suggest a clear division between the non-border provinces that depend heavily on the West for trade, capital, managerial expertise and technology (especially offshore drilling technology) and the southern border provinces where trade with China, Chinese land entrepreneurship, and Chinese migration, already represent vital components of the economic landscape. Yet this is not a particularly stable balance, since China's economic planners target the rich mineral resources of the north also. (The list of projects in the Hu-Medvedev program clearly shows this.) To counter China's growing influence, Western countries need to invest more comprehensively in the RFE, both north and south, taking advantage of China's still relatively weak investment profile in the region. To this end, the interested players might consider a coordinated investment strategy, perhaps a consortium of some kind, to pool resources, share risks, engage with relevant Russian authorities, and promote development efforts.

Finally, the United States and Russia's Far East are neighbors across the Pacific, just 58 miles apart at their closest continental points. As such, America and Russia share an objective common interest in preventing domination of the RFE – including indirect soft-power domination – by any outside power, and China is now the power in question. (For America, the Russian Far East offers the convenience of a gigantic strategic buffer between an increasingly aggressive China and the North American continent.) Russia's current alignment with China, tailored to its geopolitical ambitions in the Asia-Pacific, naturally tends to obscure this reality; and America, for its part, doesn't yet take Russia seriously as a Pacific partner, economically or strategically. Yet America's highly-touted

⁸ *Program of Cooperation between the Far East and Eastern Siberia of the Russian Federation and the Northeast of the People's Republic of China, 2009 to 2018*, pp. 13-25.

⁹ "Vladimir Putin on Foreign Policy: Russia and the Changing World," Valdai Discussion Club, February 27, 2012.

¹⁰ Ministry of Development of the Far East, "Agreement Signed on Cooperation Between the Ministry of Development of the Far East and State Development Bank of China," Khabarovsk, August 16, 2013.

“pivot” to Asia, could modify these calculations. Washington is assembling an informal coalition of Asian nations, apparently to contain China, and could eventually decide to bring Russia into the fold, at least at the margins. A more inclusive US security policy in the Pacific should benefit the RFE, inspiring greater confidence among foreign developers (non-Chinese ones) to invest in long-term projects there, thus advancing Moscow’s own modernization objectives in the region. Whether these potential synergies will be perceived as such in Moscow and Washington remains to be seen.

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