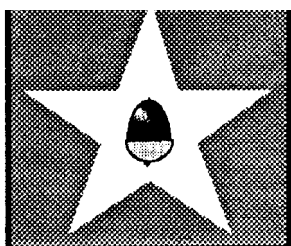


Conflict Studies Research Centre

Dr Mark A Smith

**The Russian Far East:
Drift From The Centre?**

September 2003



E112

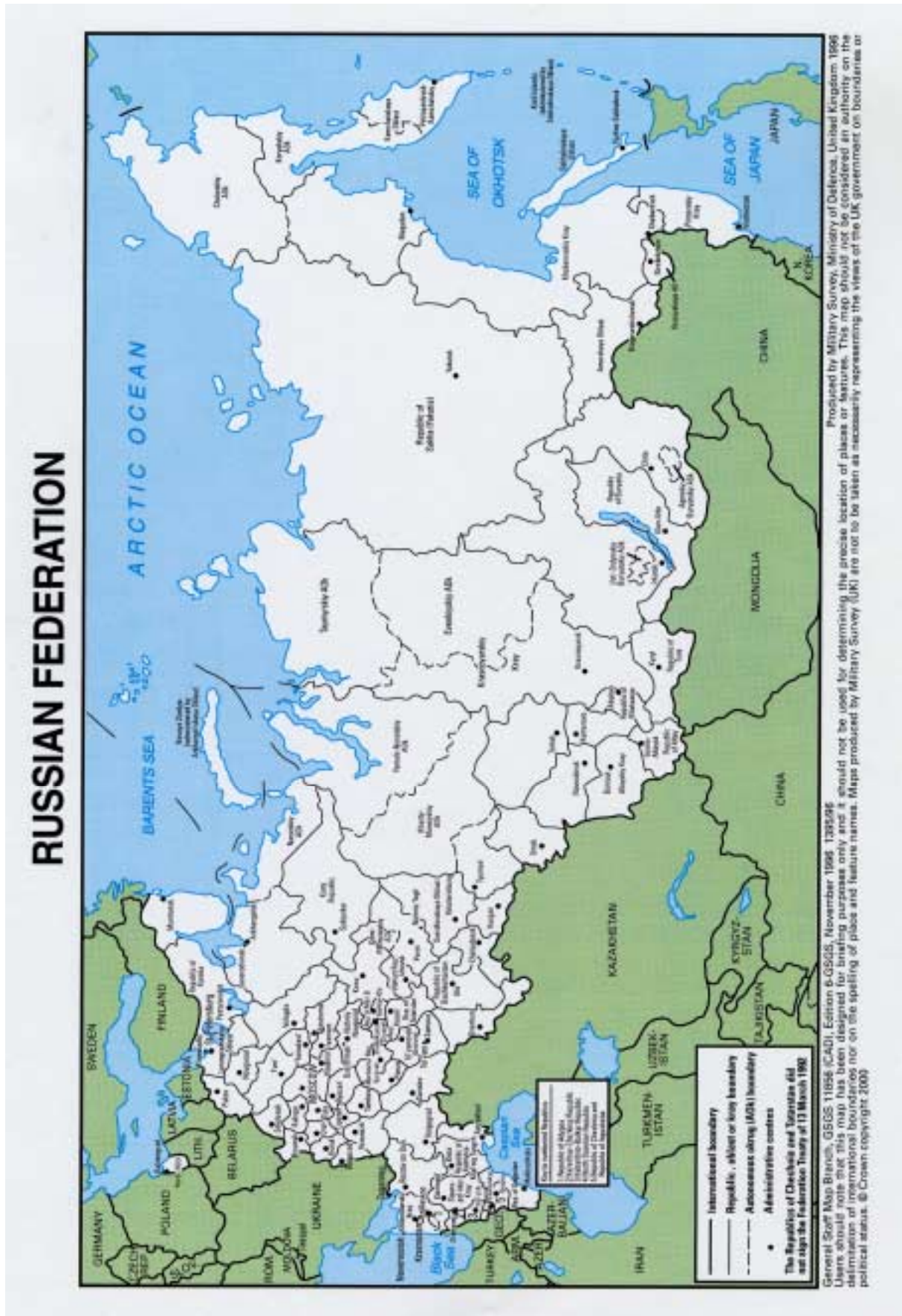
The Russian Far East: Drift From The Centre?

Dr Mark A Smith

Contents

Map: Russian Federation	2
The Region	3
Political Profile	5
Vladimir Putin's Assessment - July 2000	7
Viktor Ishayev's Assessment - May 2003	8
Ishayev's Four Scenarios	9
Foreign Interest in the Russian Far East	10
South Korea	11
China	12
Japan	14
USA	14
Future of The Russian Far East	14
Appendix 1 - Regional Fact Sheet	17
Appendix 2 - Sakhalin & Other Major Projects	19
Appendix 3 - Russian Far East - Useful Web Sites	21

Russian Federation



The Russian Far East: Drift From The Centre?

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 which will permit it to be an effective and worthy representative of Russia and implementer of her economic and political interests in this complex and most dynamic region of the world.

Viktor Ishayev, Governor of Khabarovsk kray, May 2003.¹

The Region

The Russian Far East (RFE) is currently defined as the Far Eastern Federal District. This comprises ten territories: Republic of Sakha (Yakutia); Primorskiy and Khabarovsk krais; Sakhalin, Kamchatka, Magadan, Amur oblasts; the Jewish autonomous oblast; Chukotka and Koryak autonomous okrugs. A brief overview of each can be found at Appendix 1.

The region has an area of 6.2 million square kilometres, which is just over one-third of the total area of the Russian Federation (17.075 million square kilometres). It is almost two-thirds the area of the USA (9.63 million square kilometres). However according to the 2002 census the population is 6,686,700, which is approximately 4.6 per cent of the population of the Russian Federation, which stands at 145,287,400. The biggest city in the RFE is Vladivostok (population 591,800), located 9,300 kilometres from Moscow. 76 per cent of the RFE population live in urban areas, 24 per cent in rural.

The RFE is rich in natural resources, making it an important part of the national economy. It is a producer of oil, gas, coal, diamonds, gold, silver, iron ore and various non-ferrous metals. The plenipotentiary presidential representative to the Far Eastern Federal District, Konstantin Pulikovskiy, claims that 60 per cent of the catch of the Russian fishing industry comes from the Far East. The district contains 92 per cent of Russia's reserves of tin, 81 per cent of its precious stones, 40 per cent of its gold, 23 per cent of its wolfram and 11 per cent of its coal.² There is also some manufacturing industry. Defence industries are an important part of the economies of Khabarovsk kray and Primorskiy kray. Regional domestic product comprises about 6 per cent of national GDP.³

However, although rich in natural resources, the region suffers from gross under-population, and faces continuing depopulation and lack of investment. In 1987 Soviet leader Mikhail Gorbachev promoted a Long Term Programme for the Comprehensive Development of the Far Eastern Economic Region, but this had little effect. The collapse of the Soviet Union and the centrally planned economy has exacerbated the situation.

In the Soviet era, the government provided generous subsidies in order to give citizens an incentive to live in the RFE, but as these subsidies no longer exist, the incentive to remain there has obviously lessened. The RFE economy had been artificially integrated with the western Soviet Union. This pattern of forced integration imposed high transport costs on the region's links to the outside world. Eighty per cent of imports came from elsewhere in the Soviet Union and ninety per cent of exports went to other parts of the Soviet Union. It sold raw materials at low prices and purchased manufactured goods at relatively high prices. The collapse of

the Soviet system and the possibility of developing closer ties with the global economy now mean that it makes more sense to sell raw materials on the Asian Pacific market than to other parts of the Russian Federation.

RFE manufacturing industries are uncompetitive on the world market.⁴ A 1996 study of the RFE economy by Judith Thornton identified four sectors (fishing, forest products, light industry, chemical industry) as negative value added sectors at world prices. Agriculture, ferrous metals, and coal were unprofitable.⁵ Thornton argued that fishing and timber would become unprofitable once market energy prices were introduced. The decline in defence orders in the 1990s resulted in a huge contraction of the regional machine building industry. The end of Soviet era subsidies meant that the RFE industry would have to downsize, and it was uncertain which new industries could replace them.

An increasing proportion of RFE economic production is consumed within the RFE. It has been stated that the RFE is experiencing double autarchy: increasing isolation from the Russian internal market, and increasing self-sufficiency of the sub-regional economies within the RFE. In 1990, 19 per cent of RFE economic production was destined for the internal RFE market. In 1995 this increased to 75 per cent, and by 2000 to 77.5 per cent.

The fishing industry is the biggest employer in the RFE. In 1999, it employed 17 per cent of industrial workers in Primorskiy kray, 25 per cent in Sakhalin, and 50 per cent in Kamchatka. The privatisation of the fishing industry in the 1990s led to an increase in the number of independent firms in the fishing industry, often with foreign involvement. However, the catch has declined throughout the 1990s, falling from 4.6 million tonnes in 1990 to 2.3 million in 1994. It recovered to about 3 million tonnes annually for the next four years, but fell by 350,000 tonnes in 1999. Catches fell again in 2000. However, pollock and crab stocks are being over-fished, often due to illegal fishing. Production by shoreside plants has declined by almost 60 per cent between 1990 and 1994, and shore plants and ship repair facilities are only using 20-30 per cent of their capacities. Reliable data on the RFE fishing industry is difficult to obtain, given the common practice of under-reporting catches and income. However the large number of bankruptcies and arrests of vessels by unpaid creditors indicate that the industry's health is poor.

A conference of the Primorskiy fishing industry in 1998 gave the following reasons for the state of fishing in the RFE: the end of government financial support; absence of an effective legal framework that could protect domestic producers; a deficit of operating funds for companies, plus high costs of maintaining fleets; a constant lack of quotas for harvesting seafood up to full production capacities; inadequate fish processing technology. Corruption in allocating fishing quotas and the underfunding of fisheries science are also major factors.⁶

Organised crime is a major problem in the RFE, and helps form a predominant, and not inaccurate image of the RFE as Russia's "Wild East". An APEC investment conference in September 2002 was accompanied by a number of contract killings of regional officials and business people, so undermining the conference's goal of attracting investment into the RFE. Vladimir Tsvetkov, governor of Magadan oblast, was murdered in Moscow in 2002. The commander of the Sakhalin border guard service, Vitaly Gamov, was murdered in an arson attack in 2002 after he ordered all small fishing vessels to install tracking equipment in order to curtail smuggling. The Russian mafia reportedly cooperates with the Japanese yakuza in selling stolen Japanese cars in the RFE and it also works with Chinese gangs in illegally exporting

The Russian Far East: Drift From The Centre?

timber. The share of the RFE's illegal timber trade may well be greater than the legal trade. Vladivostok has become a major drug smuggling centre.⁷

The end of the Soviet system and the lack of transport links with the rest of Russia raises the danger of the RFE becoming effectively detached from the rest of Russia, even if no formal separation takes place.⁸ A ten year programme for the development of the RFE was announced by President Boris Yel'tsin in April 1996 which envisaged spending R400 billion, but like the Soviet programme of 1987, has achieved little. In a speech in the capital of Amur oblast, Blagoveshchensk, in July 2000, Vladimir Putin acknowledged this fact and expressed concern about the RFE's demographic crisis. He warned that "I am not dramatizing the events, but if in the near future we do not make real efforts, then even the native Russian population in a few decades will mainly be speaking Japanese, Chinese and Korean".⁹ He noted that the outflow of the population was continuing, and that this raised the question of the very existence of the region as an integral part of the Russian Federation. He asked, "What sort of Far East does Russia need?" Should it be a source of raw materials, or a window into Asia in order to integrate with the Asia-Pacific region? He contended that the Far East must be considered as an integral part of Russia, but accepted that the RFE's problems lay in its vast distance from the centre, which makes its relationship with the rest of the Russian Federation the more difficult.

The 2002 census confirmed that depopulation is continuing, with people moving westward. The population in the Far East Federal District has fallen by 15.9 per cent (by more than 1 million) by comparison with data from the 1989 census (7.95 million). The regions with a significant reduction in numbers include first and foremost Chukotka Autonomous Area where the population has fallen by two-thirds, Magadan oblast (by more than half), Koryak Autonomous Okrug (37 per cent), Khamchatka oblast (25 per cent), Sakhalin oblast (20 per cent), Amur oblast (28 per cent) and Primorskiy kray (10 per cent).

Political Profile

The Russian political scientist Tamara Troyakova divides the leaders of RFE regions into three groups:¹⁰

- Economic managers, with an engineering background and experience in enterprise management and working in the CPSU structures. This group includes Viktor Ishayev, governor of Khabarovsk kray, Nikolay Volkov, head of the administration of the Jewish autonomous oblast, Vladimir Biryukov, former governor of Kamchatka, and Igor Farkhutdinov, governor of Sakhalin until his death in a helicopter accident in 2003.
- Directors. They had a career in production, usually as the director of a major enterprise. It included the late governor of Magadan oblast, Valentin Tsvetkov. Tsvetkov had sought the establishment of a free economic zone in Magadan in order to exploit its mineral resources more effectively. This group seeks more assistance from the federal centre.
- Pragmatists. These have a mixture of economic and administrative experience and had a steady career during the 1990s. The former president of Sakha, Mikhail Nikolayev, falls into this category, as does the former governor of Primorskiy kray, Yevgenniy Nazdratenko.

Regional leaderships in the RFE tend to be quite authoritarian, and there is little effective opposition to their rule. Many RFE leaders make a great play of standing up to Moscow. Most governors were born outside the RFE, but the majority had been living and working in their respective regions for several decades before entering office. They all seem to be strongly attached to their respective regions and displayed considerable hostility to Putin's reforms of centre-regional relations in 2000, when federal districts were created. The governor of Khabarovsk kray, Viktor Ishayev, is particularly hostile to Moscow. In 1998 he stated that:

While until recently there have been only a few ambitious local politicians among its adherents, now one can say that it penetrates the masses. Everywhere, among entrepreneurs, in factories, at logging-lumbering enterprises, or in mines, protests are being raised against Moscow functionaries who pump virtually all the money and resources out of the territories and never offer anything in return. Under such circumstances, the idea of 'our own' republic does not seem that absurd.¹¹

Ishayev sees himself as a leader of the RFE as a whole against Moscow, and has been especially critical of Putin's approach to centre-regional relations. He has criticised plans by the federal government to privatise the Komsomolsk-na-Amure aviation plant which manufactures Sukhoy aircraft. The headquarters of the federal district is located in Khabarovsk, and this is seen by Ishayev as a direct challenge.

Sakha under the leadership of Mikhail Nikolayev was also quite defiant of the centre. Its power sharing treaty negotiated with the central government in the Yel'tsin era gave it considerable fiscal autonomy. In June 2000 the Russian Constitutional Court ruled that the federal government owns Russia's natural resources. Since then, Moscow has attempted to regain control over the revenue from the Sakha diamond industry. In 2001 federal auditors investigated the Alrosa diamond corporation and Sakha's ownership. The Sakha government and federal government own 32 per cent of Alrosa shares. The workforce owns 23 per cent, 8 per cent belongs to Sakha local government and 5 per cent to a federal veterans' organisation. Sakha thus effectively controls 63 per cent of the shares. The federal government has attempted to gain control of 51 per cent of Alrosa's shares. In order to prevent this, Nikolayev decided to transfer the Sakha government 32 per cent stake to Sahinvest, a private fund. In 2002 the Kremlin managed to secure the election of new presidents for both Sakha and Alrosa. Sakha now has to send more than half its tax revenues to Moscow.

The Primorskiy kray leadership of Sergey Darkin is very cooperative towards the federal centre, although Darkin was not the Kremlin's preferred candidate in the 2001 gubernatorial elections. The kray is very dependent on federal subsidies (one-third of the kray's revenues come from federal subsidies), and the federal treasury funds the region's treasury directly in order to prevent regional officials misusing federal funds. The presidential plenipotentiary representative, Konstantin Pulikovskiy, claims that Darkin is the regional leader with whom he has the best relations. Governor Mikhail Mashkovtsev of Kamchatka region, which also depends heavily on federal subsidies, requested that Pulikovskiy appoint someone to facilitate cooperation between the Kamchatka administration and Pulikovskiy's office and improve the region's ability to lobby in Moscow.

The Russian Far East: Drift From The Centre?

In Chukhotka, Sibneft boss Roman Abramovich was elected as governor in December 2000. He complains that the federal government over-regulates the okrug, which hampers foreign investment and tourism. Abramovich has attempted to attract foreign investment, and in February 2002, Sibneft signed an agreement with Halliburton to provide oilfield services in exploration projects in Chukhotka.

Abramovich, Darkin and Leonid Korotkov, governor of Amur oblast constitute a new generation of pragmatic regional leaders, who seek to cooperate with the federal centre and major business groups. Sergey Darkin in particular has sought to attract Russian big business to invest in Primorskiy kray. However, many regional leaders are often hostile to foreign investment. Both the previous Nazdratenko and current Darkin administrations in Primorskiy kray have often created difficulties for foreign investors. The same is also true in Sakhalin, despite the heavy investment of foreign energy companies. The speaker of the oblast дума has called for the books of foreign oil companies to be audited, and the late governor Igor Farkhutdinov required his administration's oversight department to approve all contracts with foreign firms. The oblast administration has often given preferential treatment to local firms.

There is a strong resentment of the federal centre in the RFE, particularly since Putin's reforms have aimed more at tightening up central control over the region, rather than promoting the RFE's economic development. There does, however, appear to be a curious mix of centrifugal and centripetal sentiment throughout the region. Voting patterns in the 1999 Duma elections and 2000 presidential elections showed strong support for centripetal political forces, and regional leaders, whilst desiring greater autonomy from the centre, particularly in fiscal matters, are unlikely to seek outright secession, although they may occasionally threaten it.

	Leader	Year became Leader	Place & Date of Birth
Sakha	Vyacheslav Shtyrov	2002	Yakutia, 1953
Primorskiy kray	Sergey Darkin	2001	Primorskiy kray, 1963
Khabarovsk kray	Viktor Ishayev	1991	Kemerova oblast
Sakhalin oblast	Ivan Malakhov (acting)		
Khamchatka oblast	Mikhail Mashkovtsev	2000	Minsk, 1947
Magadan oblast	Nikolay Dudov	2003	Tula oblast, 1952
Amur oblast	Leonid Korotkov	2001	Amur oblast, 1965
Jewish autonomous oblast	Nikolay Volkov	1991	Orlov oblast, 1951
Chukotka	Roman Abramovich	2000	Saratov, 1966
Koryak autonomous oblast	Vladimir Loginov	2000	Archangel oblast, 1954

Vladimir Putin's Assessment - July 2000

In his July 2000 speech in Blagoveschensk, Putin noted that the regions within the RFE were poorly interlinked and said that the RFE and the rest of Russia must become a single organism. He noted the following key problems:

- The RFE suffers from a poor energy supply. This is the main problem for the region. Energy costs are much higher in the RFE than in other parts of Russia. He stated that the initiation of the Bureya hydro-electric station in Amur oblast (which was opened in July 2003), the gasification of Sakhaklin oblast, and Khabarovsk and Primorskiy krais must proceed, and that the distribution of oil from refineries in Khabarovsk and Komsomolsk-na-Amur needs to be rationalised.
- The infrastructure of the region is not a single entity. The main transport routes are not integrated and entire routes stand idle. The railway system is ineffective.
- The problem of poor transport links means that the fishing industry finds it difficult to send its products to its main markets in Russia. The fishing industry instead seeks foreign customers, and counts on receiving materials, finance, fuel from abroad by selling valuable fish products often at very cheap prices. It is necessary to reduce the flow of fish products abroad for processing. The entire infrastructure of RFE fishing ports must be modernised, along with the fish processing industry.
- The forestry industry faces the same dilemma as fishing. The wood processing industry needs to be modernised. Currently timber is often sent abroad for processing and the manufacture of finished products.

Putin acknowledged that the distance of the RFE from western Russia made it necessary for the region to become actively integrated into the Asian-Pacific market. He said this would serve both the economic interests of the RFE and the geopolitical interests of the Russian state, which desires to become an active player in the Asia-Pacific region. He said that Russian enterprises should operate in the Asian-Pacific market as part of the national economy of the Russian Federation. Instead, at the moment Russian fishing vessels often do not operate out of Russian ports, and Russian vessels often fly under foreign flags. Russia's share in the trade turnover in the Asian-Pacific market is only around 3-4 per cent.

Viktor Ishayev's Assessment – May 2003

In May 2003, the governor of Khabarovsk kray, Viktor Ishayev gave a pessimistic assessment of the RFE's development, showing that little progress has been made since Putin made his speech in Blagoveschensk.¹² Only 10.6 per cent of the financial obligations of the 1996 presidential programme have been met (this contrasted with 30 per cent in the 1987 USSR programme). He stated that the federal centre had no effective policy for developing the potential of the regions so that they would enhance the overall potential of the Russian Federation. In his view federal budgetary policy was not enabling regions to conduct effective economic policies. "The budget is not a stimulatory or even regulatory instrument. It is purely a fiscal instrument, which deprives regions of incentives to work effectively." Furthermore, Ishayev said, the income base of regional budgets was being reduced. In 1995 the federal budget accumulated 51.8 per cent of all incomes; by 2000 this figure stood at 55.9 per cent. The share of federal budget spending remained the same – 47.9 per cent. Regional budget spending also remained the same – 52.1 per cent. However the share of regional budget income fell from 48.2 per cent to 44.1 per cent.

The Russian Far East: Drift From The Centre?

The recession suffered by the Russian economy in the 1990s was felt particularly sharply in the RFE. In the period 1991-2002 the industrial capacity of the RFE fell by 46.2 per cent (this contrasts with 35.1 per cent for the Russian Federation overall). The volume of gross investments in the RFE over this period fell by 69 per cent (versus 66.8 per cent for the Russian Federation). In the period 1996-2001 the gross regional product shrank by 12.3 per cent and industrial production by 10 per cent. Furthermore, the RFE economy grew more slowly than the Russian economy as a whole in 1999-2001, and similarly it shrank more quickly than the Russian economy in 1996-1998.

The RFE regional economy is becoming increasingly detached from the rest of the Russian economy, so running counter to Putin's desire to see the RFE attached to the rest of Russia as a "single organism". At the beginning of the 1990s, 75 per cent of the economic output of the RFE was exported to other regions of the Russian Federation, and only 6 per cent was exported abroad. By the mid-1990s demand from the rest of the Russian Federation fell to 10 per cent of output, and exports abroad accounted for 15 per cent. In 2000, exports to the rest of the Russian Federation fell to 4.3 per cent; exports abroad rose to 18.2 per cent of economic output. The RFE economy is thus becoming ever oriented away from the rest of the Russian Federation and towards Russia's neighbours in North East Asia. It is, however, becoming merely a supplier of raw materials to its neighbours.

Ishayev's Four Scenarios

In his May 2003 assessment, Ishayev outlined four possible scenarios for the future economic development of the Far East and Baikal region. He cautioned that no one individual scenario could be utilised on its own, counselling that it would be more fruitful to combine elements of all four scenarios.

SCENARIO 1 - State support in the form of a partial re-establishment of a centralised system of redistribution of resources

The 1996 presidential programme was an attempt to realise such a scenario, but failed due to the state's inability to fulfil its spending promises. Putin's own programme for the region for the period 2002-2010 aims at spending considerably less money than envisaged in the 1996 programme, and so will also not enable this first scenario to be realised. Compared with federal spending on other regional programmes in 2003, the Far East and Baikal region receives less than Tatarstan, Bashkortostan, and Southern Russia.

SCENARIO 2 - Traditional export specialisation on the basis of long-term exploitation of natural resource potential

In 1990 energy and raw material production comprised 32.4 per cent of industrial output of the RFE. By 2001 it stood at 60.3 per cent. The scenario would result in the RFE remaining no more than a raw materials appendage of the Asia Pacific region.

SCENARIO 3 - Active economic cooperation with China, with the aim of integrating with the markets of the Asia Pacific region

Ishayev notes that cooperation with China poses serious challenges and possibly threats for the RFE. He is concerned that the Chinese leadership is aiming at the secret conquest of far eastern and Siberian territories, by settling Chinese communities there and following this by forming

administrative-territorial autonomies. He is concerned that the border demarcation process could enable China to maintain its claims to Russian territories. The current Chinese population in the RFE is about 150,000 to 200,000, but there are concerns that many Chinese are overstaying their visas and remaining illegally in the RFE.¹³

However, China's importance as an economic actor in the RFE is unavoidable. China is the RFE's biggest trade partner, accounting for 42 per cent of the RFE's foreign trade, although it is not so far a serious investor. Ishayev sees cooperation in the energy sector as the most promising area of the RFE-Chinese economic relationship, particularly in the extraction of gas, oil and coal. He calls for the development of large scale projects between the two states, arguing that Russian natural resources and high technologies could combine with a cheap Chinese labour force that is quickly becoming more skilled. This scenario would require the coordination of a long-term strategy with China, and Russia would need to create highly attractive conditions in the RFE to attract foreign investment.

SCENARIO 4 - The formation of an open economy, participating in global integration processes

This requires closer economic cooperation not only with China, but also with the USA and Japan, the aim being to develop Russian industry and overcome her role of being merely a raw materials supplier.

Both the federal and various regional leaderships would probably prefer a mixture of all four scenarios, albeit with different emphases. That is, the state would prefer minimal support from the centre, but greater control over tax revenues generated in the regions, and the regions greater support from the centre, but with greater regional fiscal autonomy. Neither side is happy with the current balance, which means that there is considerable disaffection in the relationship. Both support the RFE's integration into the global economy, but differences between them over fiscal policy make it difficult for the RFE to integrate in a way that will enable her to move beyond being a raw materials supplier.

Foreign Interest In The Russian Far East

Increased interaction with major economic powers of the Asia Pacific region is seen both by regional leaderships and by Moscow as essential if the RFE is to have any hope of overcoming its economic problems and thereby provide incentives for its population not to migrate to other parts of the Russian Federation.

The levels of foreign investment in the RFE have been low in comparison with other regions of the Russian Federation. The only exception has been Sakhalin, due to the oil and gas projects there. These are detailed in Appendix 2. In 2001, the RFE received \$767 million in foreign investment.¹⁴ The major economic partners of the RFE are the USA, Japan, China and South Korea, as the following tables show:

The Russian Far East: Drift From The Centre?

The geographical structure of RFE exports:

	(%)
China	26.8
Japan	20.2
South Korea	17.7
Singapore	11.8
USA	6.6
Others	16.9

The geographical structure of the RFE imports:

	(%)
China	26.5
South Korea	20.1
USA	16.5
Japan	12.1
Others	24.8

Source: Viktor Ishayev, Development Strategy of the Far East in a changing world, May 2003.

Foreign Investment in Key Regions in the Russian Far East (US\$m)

Region	2000	2001
Sakhalin	251	388.9
Yakut Sakha	160	144.6
Primorskiy kray	78	108.6
Kamchatka	29	78.4
Khabarovsk kray	27	19.1

Source: Tamara Troyakova & Elizabeth Wishnick, Integration or Disintegration? Challenges for the Russian Far East in the Asia-Pacific Region, June 2003, p15.

South Korea

South Korea's cumulative investment in the Russian Federation stood at \$154 million at the end of 1999.¹⁵ By contrast, her cumulative investment in China at the end of 1999 was \$4.33 billion. Prior to the establishment of diplomatic relations between the USSR and South Korea in 1990, several large South Korean corporations proposed large-scale investment projects. Many of these were to be located in the RFE. Geographically, South Korea's main investments in Russia are concentrated in the Far East, Moscow and East Siberia. The main sectors of South Korean investment are mining, metallurgy, hotels, and the food industry, including fishing. Primorskiy kray is the main area in which South Korean capital is invested: the region received over \$33 million from South Korean investors by the mid 1990s. Some of the main investments are:

- Hyundai has concluded contracts in fisheries, forestry, natural gas and minerals. Hyundai owns 50 per cent of the Svetlaya timber processing plant in Primorskiy kray. In 1997 Hyundai invested \$102 million in developing a large hotel-office complex in Vladivostok.

- In 2000, eight Korean businesses and associations were engaged in agricultural production in Primorskiy kray. South Korean companies intend to produce rice, corns, beans and other crops. Clothing manufacturers are producing clothes in the RFE and exporting them to the USA to bypass US quotas imposed on South Korean clothing imports. The US-South Korean owned S H International makes T-Shirts and sweatshirts in the RFE and sells them in the USA.
- A major Korean industrial complex has been set up in the Nakhodka Free Economic Zone (NFEZ) in Primorskiy kray. This complex was first discussed in 1992, a preliminary agreement was reached in 1994 and a final agreement was signed during President Kim Dae Jung's visit to Moscow in 1999. The agreement initially called for a lease of 3.3 million square metres of land in the NFEZ by the Korea Land Corporation (KLC) for 49 years; South Korean companies would rent lots from the corporation and participate in the construction of a "technology park." However the KLC will now just build a complex covering 200,000 square metres.
- The South Korean Gas Corporation (KOGAS) has been involved in a study to build a gas pipeline from Yakutia through North Korea to South Korea. However KOGAS decided against a full feasibility study because of the project's low profitability. In December 1997, South Korea, China, Japan, Russia and Mongolia signed an agreement to advance the development of gas fields in Siberia. In 1999 Russia Petroleum and the Chinese National Petroleum Corporation signed a general agreement on a feasibility study of the Kovykta gas fields. KOGAS joined this Russo-Chinese agreement in November 2000, having conducted its own feasibility study in 1996-97. If a decision is made to go ahead with the project, then a pipeline would link Irkutsk, Beijing and possibly Pyongyang near Seoul. The cost has been estimated at \$12 billion, and another feasibility study is underway, due to be completed at the end of July 2003. The pipeline would have a planned capacity of 2.9 billion cubic feet per day (Bcf/d), of which China would likely consume about 1.9 Bcf/d and South Korea 1 Bcf/d. The main foreign backer of the project is BP, which owns a 30% stake in Russia Petroleum, the licence holder for the Kovykta gas field. Due to tensions on the Korean peninsula, the route currently under consideration for the section of the pipeline to South Korea would bypass North Korea by running undersea from the port of Dalian in China to the South Korean coast near Seoul. The new route would also bypass Mongolia.¹⁶

China

China is the RFE's main trade partner. Amur oblast and Khabarovsk kray are heavily dependent on Chinese trade. In 2002, China accounted for 43 per cent of Khabarovsk kray's exports and 29 per cent of imports, making it the kray's biggest trade partner. In 2002, China accounted for 74 per cent of Amur oblast's foreign trade turnover.

The RFE and Chinese economies complement each other. The RFE is rich in natural resources such as oil, gas and timber which China does not have in sufficient quantities, and Heilongjiang province is able to provide oil refining and wood processing. It is cheaper for the RFE to import food and consumer goods from northern China than from European Russia. The RFE can also provide China with

The Russian Far East: Drift From The Centre?

military equipment and other high technologies. So far, however, this economic compatibility has not been fully exploited.

Much trade comes from Chinese shuttle traders. There have been complaints about the poor quality of Chinese goods, although the flow of Chinese goods to Russia has increased since the 1998 financial crisis made high quality imports from other countries very expensive. China has two trade centres in Moscow to display Chinese goods and plans to set up another one in Khabarovsk. The cross border relationship has suffered in 2003 as a result of the SARS epidemic in China. Russia closed most border crossing points in May, and several air routes have been closed.

The most important sectors of the RFE-Chinese economic relationship are energy and arms sales. In order to supply China's increasing oil demand and boost its own export potential, Russia has been negotiating with China to build an oil pipeline linking the two countries. In July 2000, President Putin and President Jiang Zemin signed a memorandum of understanding on a feasibility study for a potential oil pipeline between Russia and China, and in September 2001 Russian and Chinese officials signed a general agreement to prepare a feasibility study for the line's construction.

Originally, Transneft and Russia's second largest oil producer, Yukos, were working together on the idea of building the proposed \$1.7 billion pipeline, which would bring East Siberian oil to northeastern China. Under a 25-year deal, the pipeline would supply China with 400,000 bbl/d starting in 2005 - the equivalent of 26% of China's projected net imports at that time. Spur lines would eventually link the Talakanskoye, Verkhne-Chonskoye, and Yurubchenskoye fields to the main pipeline, boosting capacity to 600,000 bbl/d by 2010 and helping to alleviate localized fuel shortages in Russia that have been aggravated by high rail tariffs.

A preliminary proposal signed by Chinese and Russian sides called for the line to stretch nearly 1,500 miles from Angarsk, across Mongolia, then into Beijing. Russia wants to cut the pipeline's distance by traversing Mongolia, but China would like to circumvent Mongolia for security reasons. In addition, Yukos and Transneft have differed in their preferences for the pipeline route, with Yukos, which previously favoured a route from its fields in the Tomsk region straight to China, now favouring one that would terminate in Nakhodka on Russia's Pacific coast. Yukos argues that shipping crude oil via Nakhodka would give producers a bigger choice of buyers, while Transneft has said that both routes could eventually be built. A feasibility study for a 400,000bbl/d-capacity pipeline linking East Siberia with Dalian in northeastern China was due in the first half of 2003.

Transneft's plan would take Russian crude from both West Siberia and East Siberia via a 1 million bbl/d pipeline to an export terminal at Nakhodka. China presumably would be one of the major consumers of oil from such a project, but it would also give Russia increased access to the Japanese, South Korean, and other East Asian markets.¹⁷ In March 2003 Prime Minister Mikhail Kasyanov said that the Russian government had chosen the combined Angarsk-Nakhodka project with a branch running to Daqing.

China is Russia's main weapons customer, and several major orders have been made from RFE enterprises. The Komsomolsk-na-Amur aviation plant is the main supplier of Sukhoy-27 aircraft to China.

Japan

Japan is a major trading partner of the RFE.¹⁸ In 1997, one-third of RFE exports went to Japan. Major Russian exports to Japan include non-ferrous metals, timber, fish products and energy. One of Japan's major exports to the RFE has been secondhand cars. In order to develop trade, the Japan External Trade Organisation and the Japan Association for Trade with Russia and East Central Europe have established training centres for small and medium sized enterprises in the RFE. Japan has participated in the renovation of airport terminals in Vladivostok, Khabarovsk and Yuzhno-Sakhalinsk. In May 1999 the Primorskiy kray administration and the Japanese-Russian business committee signed an agreement according to which Japan would invest \$10 million to build new facilities for grain storage, wood chip processing and container transshipment.

Japan has invested \$40 million in a floating low-radiation liquid waste processing complex at the Zvezda facility in Bolshoy Kamen, a submarine base in Primorskiy kray. Japanese enterprises have also invested in timber processing centres in Primorskiy kray and Khabarovsk kray. Japan has also been a major investor in energy projects in Sakhalin. Japan is heavily dependent on Russian aluminium exports, but Russian coal has been losing out in price competitiveness to Australian coal. Russian timber is also losing its attractiveness to the Japanese market.

USA

The USA has been especially interested in the development of Sakhalin's energy reserves.¹⁹ Sakhalin is the major target for US investment in Russia after Moscow. US capital has also been invested in gold mining in Magadan, timber in Khabarovsk kray, and defence conversion, communications, fishing and transport in Primorskiy kray. There is a Coca-Cola bottling plant in Vladivostok.

Several US-Russian programmes have been set up to promote economic relations between the USA and RFE. The Russian-American Pacific Partnership links the West Coast states of the USA with the territories of the RFE.²⁰ The American-Russian Centre at the University of Anchorage in Alaska runs training programmes to develop entrepreneurship in the RFE.²¹

Future Of The Russian Far East

None of the major problems faced by the RFE has diminished since the end of the Soviet period. In fact, they have worsened. The problems of depopulation, lack of investment, the inadequate transport links with western Russia and the prospect of becoming little more than a raw materials supplier to Russia's Asian Pacific neighbours have become more rather than less acute since 1991.

The state lacks either the means or the will to fulfil large federal programmes. However, without state support the RFE's problems will remain. There has been some progress. The construction of the Bureya hydro-electric station (which was opened by Putin in July 2003) will improve the electricity supply and should equalise the cost of electricity in the region with the rest of the Russian Federation. This should do much to reduce power cuts, which have been a major problem in the RFE for several years. In some cases, power supplies to the Pacific Fleet have been cut because of non-payment of bills. The completion of the Chita-Khabarovsk motorway, scheduled for the end of 2003-start of 2004 will improve transport links with the western regions of the country.

The Russian Far East: Drift From The Centre?

However, these measures will not in themselves overcome the problem of a drift away from the federal centre. This does not mean that it is likely that the region would ever attempt to formally separate from the rest of the Russian Federation.²² However it does mean that the federal centre's desire that the region be part of a single economic organism with western Russia is increasingly unlikely to be fulfilled if the state is unable to implement large scale spending to develop infrastructure and transport links. It will be difficult to attract investment in the absence of an adequate transport and communications system. Lack of investment will continue to hold the region back economically, which means that depopulation is also likely to continue.

The region's post-Soviet economic orientation towards the Asia-Pacific region is the most logical option. It does carry the risk of the region becoming and remaining a raw materials supplier to technologically more advanced neighbouring states, but there would appear to be little alternative. Moscow cannot provide the necessary means, and neither can it force the local Russian population to remain in place. If income from raw materials exports increases regional wealth, then this would appear to be the best way to enhance the RFE's attractiveness to its population. Permitting regional governments a wide degree of autonomy in forming legislation to attract foreign capital would also appear to be one of the most promising means of encouraging the RFE's economic development and hopefully to move beyond simply extracting raw materials.

In many cases, however foreign enterprises in the RFE have been deterred by high tax levels imposed by the federal government. South Korean enterprises, for example, have been put off, and although Russia has promised tax breaks for the Nakhodka free economic zone, they have not so far been acceptable to the South Korean side. Thus what may have been a "motor" for Primorskiy kray's economic development has not been realised. If regional governments were to be permitted a higher degree of autonomy they too would have to develop a less suspicious attitude towards foreign investment. However, the centre is unlikely to permit the RFE such autonomy. It runs against the centralising trend in Putin's approach towards centre-regional relations.

This may mean that the federal government would have to accept a high degree of de facto autonomy in the RFE, and possibly increased economic dependence on the RFE's foreign neighbours. The only alternative is continued stagnation and population outflow, which in itself increases the long term possibility of large-scale Chinese settlement of the RFE, so realising the fears of Khabarovsk kray governor Viktor Ishayev. The centre will not willingly abandon sovereignty over the RFE. The Russian leadership desires that Russia be an Asian-Pacific power, as well as a European one, so it wishes to maintain a military presence in the Far East and Pacific, and does not wish to lose the mineral resources of the RFE. If this region were to begin moves to secede from the Russian Federation, then this would increase the likelihood of intervention by neighbouring powers (particularly China) in an attempt to gain control of the RFE's natural resources. The most likely outlook is a continuation of the status quo, with some measures being taken by the federal government to support the region, limited foreign investment, and attempts by regional governments to maintain an economic relationship with China, but to avoid excessive Chinese immigration.

ENDNOTES

- ¹ *Development Strategy of the Far East in a changing world*, <http://www.adm.khv.ru/invest2.nsf>.
- ² Konstantin Pulikovskiy, "We have huge potential", *Dal'nevostochnyy Federal'nyy Okrug Obshchestvenno-Politichesky Zhurnal*, vypusk 9, <http://www.dvfo.ru>.
- ³ See the website of the presidential plenipotentiary representative to the Far Eastern Federal District, which gives information on the economies of the territories of this district, <http://www.dfo.ru>.
- ⁴ See Judith Thornton & Charles E Ziegler, 'The Russian Far East in Perspective', in Judith Thornton & Charles E Ziegler eds, *Russia's Far East: a region at risk*, Seattle & London, The National Bureau of Asian Research in association with University of Washington Press, 2002, pp3-34.
- ⁵ *Ibid*, p6.
- ⁶ For a discussion of the fishing industry see Judith Thornton, 'The Exercise of Rights to Resources in the Russian Far East,' in Michael J. Bradshaw ed. *op cit.* pp.111-117, and Tony Allison, 'The Crisis of the Region's Fishing Industry: Sources, Prospects, and the Role of Foreign Interests,' in Thornton and Ziegler, *op cit.*, pp.139-164.
- ⁷ See Troyakova and Wishnick *op cit.*
- ⁸ See the interview with governor of Khabarovsk kray Viktor Ishayev in *Nezavisimaya Gazeta*, 18 November 2002. See also his speech entitled *Strategiya razvitiya Dal'nego Vostoka v izmenyayushchemsya mire*, 6 May 2003 which appears on the website of the administration of Khabarovsk kray, <http://www.adm.khv.ru/invest2.nsf>.
- ⁹ Thornton & Ziegler, *op cit.*, p7. The full text of the speech appears on the Russian Presidential website. See the archives for 21 July 2000: <http://president.kremlin.ru/text/appears/2000/07/28796.shtml>.
- ¹⁰ See Tamara Troyakova, 'The Political Situation in the Russian Far East,' in Michael J. Bradshaw, *The Russian Far East and Pacific Asia: unfulfilled potential*, Richmond, Curzon Press, 2001, pp.51-72, and Tamara Troyakova and Elizabeth Wishnick, *Integration or Disintegration? Challenges for the Russian Far East in the Asia-Pacific Region*, June 2003 on which this section is based.
- ¹¹ *Ibid.*, p.51-52
- ¹² See Ishayev's speech entitled *Strategiya razvitiya Dal'nego Vostoka v izmenyayushchemsya mire*, 6 May 2003, <http://www.adm.khv.ru/invest2.nsf>.
- ¹³ See Tamara Troyakova & Elizabeth Wishnick, *Integration or Disintegration? Challenges for the Russian Far East in the Asia-Pacific Region*, June 2003, pp30-32, <http://src-h.slav.hokudai.ac.jp/jp/seminors/src/troyakova-wishnick.pdf>.
- ¹⁴ See Troyakova & Wishnick, *op cit.*, for more detailed information on the economic interests of major powers in the RFE. See also Ishayev, as cited in Fn. 7.
- ¹⁵ See Seung-Ho Joo, "Economic Relations between South Korea and Russia", in Thornton & Ziegler eds, *Russia's Far East*, p441-470.
- ¹⁶ See US Department of Energy Country Analytical Briefs for China, <http://www.eia.doe.gov/emeu/cabs/china.html>.
- ¹⁷ See US Department of Energy Country Analytical Briefs for Russia <http://www.eia.doe.gov/emeu/cabs/russia.html>
- ¹⁸ See Kunio Okada, "The Japanese Economic Presence in the Russian Far East", in Thornton & Ziegler, eds, *Russia's Far East*, pp419-440.
- ¹⁹ See the website of the US Department of Commerce dealing with the Russian Far East, <http://www.bisnis.doc.gov/bisnis/country/fareast.cfm>, and Judith Thornton, "Sakhalin Energy: Problems and Prospects", in Thornton & Ziegler, eds, *Russia's Far East*, pp165-192.
- ²⁰ See <http://www.ahwg.org/>. See also the website of the Foundation for Russian-American Economic Cooperation, <http://www.fraec.org/>.
- ²¹ See <http://www.arc.uaa.alaska.edu/>.
- ²² The former governor of Primorskiy kray, Yevgenny Nazdratenko, once warned that a Far Eastern Republic could be declared, although he opposed such a move. See his interview "Let's have the opportunity to develop", *Nezavisimaya Gazeta*, 19 March 1996.

Appendix 1 - Regional Fact Sheet

Republic of Sakha

Area: 3,103,200 square kilometres

Population: 948,100 (Yakut 33.4 per cent; Russians 50.3 per cent; Ukrainians 7.1 per cent; 2.3 per cent peoples of the north, including Eveny, Evenky and Yukagiri)

Capital: Yakutsk

President Vyacheslav Shtyrov elected January 2002

Main features of the economy: mining (precious stones, gold, tin, mica, wolfram, iron ore, coal); gas production; timber

Primorskiy kray

Area: 165,900 square kilometres

Population: 2,068,200 (Russians 83 per cent; Ukrainians 8 per cent; Belarusians 1 per cent)

Capital: Vladivostok

Governor Sergey Darkin elected June 2001

Main features of the economy: fishing; engineering and manufacturing (aircraft production); shipbuilding and repair; timber; non-ferrous metallurgy

Khabarovsk kray

Area: 824,600 square kilometres

Population: 1,435,400 (Russians 86.4 per cent; Ukrainians 6.1 per cent, Belarusians 1.1 per cent, Tatars 1.0 per cent, Nanaytsi 0.7 per cent, Jews 0.3 per cent)

Capital: Khabarovsk

Governor Viktor Ishayev appointed December 1991

Main features of the economy: engineering (shipbuilding; aircraft; trains); ferrous metallurgy; timber; mining (coal, non-ferrous metals)

Sakhalin oblast

Area: 87,100 square kilometres

Population: 546,500 (Russians 81.6 per cent, Ukrainians 6.5 per cent, Koreans approx 5 per cent, Belarusians 1.6 per cent, Tatars 1.5 per cent, Mordovians 0.8 per cent, peoples of the north – Nivkhi 0.28 per cent, Orochi 0.03 per cent, Evenki 0.03 per cent)

Capital: Yuzhno-Sakhalinsk

Governor Igor Farkuthdinov appointed April 1995. Killed in a helicopter crash in August 2003. Deputy governor Ivan Malakhov is acting governor. Gubernatorial elections are scheduled for December 2003.

Main features of the economy: fishing, forestry, oil, gas, coal

Khamchatka oblast

Area: 472,300 square kilometres

Population: 358,800

Capital: Petropavlovsk-Kamchatsky

Governor Mikhail Mashkovtsev elected December 2000

Main features of the economy: fishing; timber; shipbuilding

Magadan oblast

Area: 1,199,100 square kilometres

Population: 182,700 (Russians 75.2 per cent; Ukrainians 14.9 per cent; Belarusians 1.9 per cent; Tatars 1.5 per cent; Chukchi 0.2 per cent; Jews 0.2 per cent; Eveny 0.6 per cent; Koryaki 0.2 per cent; Yakuts 0.2 per cent; others 5.1 per cent)

Capital: Magadan

Governor Nikolay Dudov elected February 2003, replacing Valentin Tsvetkov (murdered October 2002).

Main features of the economy: mining: gold, silver, tin, wolfram, coal; fishing

Amur oblast

Area: 363,700 square kilometres

Population: 902,500 (Russians 86.8 per cent, Ukrainians 6.7 per cent, Belarusians 1.7 per cent, Tatars 0.8 per cent)

Capital: Blagoveshchensk

Governor Leonid Korotkov elected April 1991

Main features of the economy: mining gold, coal, iron ore, quartzite, caoline, tufa, limestone; forestry; engineering

Jewish Autonomous Republic

Area: 36,000 square kilometres

Population: 190,900 (Russians 83.2 per cent, Ukrainians 7.4 per cent, Jews 4.2 per cent)

Capital: Birobidzhan

Governor Nikolay Volkov elected December 1991

Main features of the economy: engineering (agricultural machinery); forestry

Chukotka Autonomous Area (formerly part of Magadanskaya oblast)

Area: 737,700 square kilometres

Population: 53,600 (Russians 66 per cent, Ukrainians 15 per cent, northern peoples 13 per cent – Chukchi, Eveny, Eskimos, Chuvantsy, Yukagiri)

Capital: Anadyr' (10,000)

Governor Roman Abramovich elected December 2000

Main features of the economy: mining (gold, tin, wolfram, coal, mercury)

Koryak Autonomous Territory (formerly part of Khamchatka oblast)

Area: 301,500 square kilometres

Population: 25,000 (Russians 62 per cent, Koryaki 16.4 per cent, Ukrainians 7.2 per cent, Chukchi 3.6 per cent, Itelmeny 3 per cent)

Capital: Palana

Governor Vladimir Loginov elected December 2000

Main feature of the economy: fishing

Appendix 2 - Sakhalin & Other Major Projects

A 1997 study estimated Sakhalin's total recoverable reserves of oil, gas and condensate at 99.6 million tons of oil equivalent onshore, and 791 million tons on the Sakhalin shelf. This is more than half the size of reserves in Alaska's Prudhoe Bay. In 1999 the Sakhalin energy sector was the second largest recipient of foreign investment in Russia after Moscow. Production-sharing agreements (PSA) are the basis for these multinational projects.

Project	Participants	Capacity	Cost	Notes
Sakhalin 1 (Chayvo, Odoptu, Arkutun-Dagi)	ExxonMobil (30%), SODECO (consortium of Japanese companies) (30%), Rosneft (20%), ONGC Videsh Ltd (India) (20%)	17.1 Tcf (trillion cubic feet) at Chayvo, Odoptu, and Arkutun-Dagi fields	-	Drilling and appraisal continuing; first oil expected in 2003, predicted peak of 200,000 bbl/d
Sakhalin 2 (Sakhalin Energy Investment Co Ltd)	Royal Dutch/Shell (62.5%, operator), Mitsui (25%), Mitsubishi (12.5%)	4 billion barrels of oil and more than 20 Tcf of gas at Piltun-Astokhskoye (PA) and Lunskoye fields	\$1.1 billion for Phase I; \$8.9 billion for Phase II	Producing approximately 90,000 bbl/d at PA; Phase II set to begin (construction of liquefied gas facility, development of offshore fields)
Sakhalin 3 (Kirinskiy)	ExxonMobil, Texaco, Rosneft-SMNG	Ayyash and Eastern Odoptu fields	\$13.5 billion	PSA pending
Sakhalin 4	Rosneft (50%), Rosneft-SMNG (50%)	3.53 Tcf of gas at the Astrakhanovskiy block	Will need an estimated \$2.6 billion to develop	Will need an estimated 6 years to explore; PSA pending
Sakhalin 5	BP, Rosneft will tender jointly	Estimated 4.4 billion barrels of oil and 21 Tcf of gas in the East Schmidtovskiy blocks	-	-
Sakhalin 6	Rosneft, ExxonMobil, and Texaco will tender jointly	-	-	-
China Natural Gas Pipeline	China National Petroleum Corp, Republic of Sakha; Gazprom may act as operator	Approximately 1,700-mile pipeline, Chayandinovskoye gas field to Xinjiang, (about 550 miles southwest of Beijing in northern China); planned capacity of 423-706 Tcf per year	Estimated \$6 billion to \$10 billion	Preliminary agreement signed
China-South Korea Natural Gas Pipeline	BP (UK), Tyumen Oil (Russia)	2,000-2,700-mile pipeline from Kovykta gas field in Irkutsk to	Estimated \$6 billion to \$10 billion	Preliminary agreement signed, several routes being discussed

		northeastern China (possibly via Mongolia), terminating in South Korea via a sub-sea pipeline across the East China Sea		
China Oil Pipeline	Yukos, Transneft, China National Oil Corp	1,400 to 1,500-mile pipeline from Angarsk (East Siberia) to Beijing, potentially via Mongolia; Initial 400,000-bbl/d capacity, eventually rising to 600,000 bbl/d by 2010	Estimated \$2.5 billion	Preliminary agreement signed; feasibility study due first half of 2003, several routes being discussed
Japan Natural Gas Pipeline	ExxonMobil, SODECO (consortium of Japanese companies)	120-mile pipeline proposed from the Sakhalin I field to Sapporo, on Japan's northernmost island of Hokkaido; pipeline could be extended to Tokyo	-	Feasibility study being conducted

Appendix 3 - Russian Far East - Useful Web Sites

<http://www.dfo.ru> - website of the Presidential Plenipotentiary Representative of the Far Eastern Federal District. Contains information on the region as a whole, plus the individual territories. It also contains an on-line magazine, <http://www.dvfo.ru>

<http://www.bisnis.doc.gov/bisnis/country/foreast.cfm> - website of the US Department of Commerce devoted to the RFE. Contains a list of websites: http://www.bisnis.doc.gov/bisnis/country/030221web_rfe.htm

<http://vlast.rambler.ru/8620/8633/> - contains information on the region as a whole, plus the individual territories.

Websites of the regional governments:

Republic of Sakha (Yakutia) - <http://www.sakha.ru/>

Primorskiy kray - <http://www.primorsky.ru/>

Khabarovsk kray - <http://www.adm.khv.ru/invest2.nsf>

Sakhalin oblast - <http://www.adm.sakhalin.ru/>

Khamchatka oblast - No web site

Magadan oblast - <http://www.magadan.ru/>

Amur oblast - <http://www.amurobl.ru/>

Jewish autonomous oblast - <http://www.eao.ru/>

Chukotka autonomous okrug - <http://www.chukotka.org/>

Koryak autonomous okrug - No web site

Disclaimer

The views expressed are those of the
Author and not necessarily those of the
UK Ministry of Defence

ISBN 1-904423-47-7

Published By:

Defence Academy of the
United Kingdom

Conflict Studies Research Centre

Haig Road
Camberley
Surrey
GU15 4PQ
England

Telephone: (44) 1276 412995

Fax: (44) 1276 686880

E-mail: csrc@defenceacademy.mod.uk

<http://www.csrc.ac.uk>

ISBN 1-904423-47-7