



A REGION WITH SPECIAL NEEDS

THE RUSSIAN FAR EAST IN MOSCOW'S POLICY

Szymon Kardaś, additional research by: Ewa Fischer

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CENTRE FOR EASTERN STUDIES

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THESES

1. While the Russian Far East was not an important region in the Russian central government's internal policy during the 1990s, when Vladimir Putin assumed the presidency it was declared strategically significant. Intensified interest in the region became possible mainly as a result of the improvement of the economic situation in Russia, which was itself linked to the boom in prices on oil and gas markets. However, regardless of the numerous strategies, concepts and programmes adopted, the Russian government over the past 25 years has been unable to develop a genuinely comprehensive model for the region's development.
2. Considering the concrete measures taken by the Russian government, energy and transport need to be recognised as the region's most promising sectors. On the one hand, one direct consequence of the priorities signalled by the government will be that the state passes the burden of investing in the region to such strategic Russian companies as Rosneft, Gazprom and RZD (Russian Railways) which are engaged in the implementation of expensive infrastructural projects in the Russian Far East. On the other hand, this will result in a deepening reliance of the Russian and regional economies on the energy sector, which is increasingly sensitive to the changing situation on external markets.
3. Moscow has been unable so far to generate tangible development impulses in the region, so the Russian Far East has not yet become – contrary to the goals set – an important instrument for strengthening Moscow's economic influence in East Asia. The expectations that cross-border economic co-operation would intensify to an extent that could significantly improve the dynamics of regional development have not been fulfilled. The actual engagement of foreign capital, predominantly Chinese, is much lower than declared at the time of top-level diplomatic meetings.
4. The main barriers to development are those linked to systemic problems existing in Russia as a whole, including above all the lack of a coherent concept of economic development and the ineffective governance system. Furthermore, the significant distance from the European part of the Russian Federation and the poorly developed transport routes adversely affect economic contacts between the Far East and other Russian regions. Nevertheless, many barriers have a specifically local character: staffing problems, the decentralised energy system and the limited engagement of foreign investors.

5. At present, there is no risk that the region will be as marginalised as it was in the 1990s. At the same time, there are no prerequisites that would permit the assumption that the economy of the Russian Far East could become competitive in relation to the increasingly rapidly developing northern provinces of China or South Korea and Japan in the medium or long term. Therefore, it appears that political reintegration of the region with the centre, tighter institutional control of the region by Moscow and newly established institutions, nominations for local officials and adopted strategies, and its status as a stable supply base of raw materials for Asian countries is, in the current circumstances, the maximum development potential of the Russian Far East.

INTRODUCTION

The goal of this paper is, on the one hand, to analyse the evolution of the programme conceived by the federal government for the development of the Russian Far East (in this paper, the term is equivalent to the territory of the Far Eastern Federal District, FEFD), and, on the other hand, to evaluate the specific actions taken by the government indicating the best-developed economic sectors of the region and by identifying the systemic barriers hindering its development.

The statistical data provided in this paper concern, above all, the Far Eastern Federal District. However, in certain cases collective data covering the FEFD and the so-called Baikal Region, which is part of the Siberian Federal District, have been used (this is indicated clearly in the text).

I. THE SPECIAL CHARACTERISTICS OF THE RUSSIAN FAR EAST AND THE EVOLUTION OF THE CONCEPT FOR ITS DEVELOPMENT

The collapse of the USSR severely affected the residents of the Russian Far East and its economy where the mining and defence sectors and heavy industry predominated. The region, which for years had supplied raw materials and processed products and yet had also benefited from significant subsidies from the federal budget, was forced to solve local problems by itself, which adversely affected its further development. The region's economic ties with the remaining part of Russia weakened. Trade with the rapidly developing neighbouring Asian countries began to grow at a faster rate than internal regional trade. This triggered increasing problems with ensuring social stability in the Russian Far East and with its cultural identity.

The situation changed after Vladimir Putin took power, especially in the previous years, when the Russian government announced a political and economic 'turn to the East'. Actions were taken to reconstruct and stimulate the region whose unique geographical location and significant potential (albeit partially untapped) in the areas of raw material supplies and defence gives it great geopolitical and economic importance. In his speech in December 2013, President Vladimir Putin announced that the development of Eastern Siberia and the Far East was the national priority in the 21st century, hoping that it would become a driving engine for Russian economic growth in the coming decades. The region, according to the Russian government's assumptions, was intended to become both a raw material base for the neighbouring Asian countries (above all China) and also an investment destination, which would contribute to its economic revival. One confirmation of the Russian plans is provided by documents adopted over the past decade or so, such as the Strategy for Socio-Economic Development of the Far East and the Baikal Region to 2025 (2009) and the Transport Strategy of the Russian Federation to 2030 (2014). In 2014, the government also approved the Concept for Socio-Economic Development of the Kuril Islands (Sakhalin Oblast) for 2016–2025. In 2012, the Ministry for Development of the Russian Far East was established, which initiates, coordinates and supervises the implementation of the programmes.

1. General characteristics of the Russian Far East

The Russian Far East has an area of nearly 6.2 million km², which is 36.1% of the area of the Russian Federation. In the present administrative division of

Russia into federal districts, the Far Eastern Federal District encompasses the Sakha Republic (Yakutia), the Primorsky, Khabarovsk and Kamchatka Krai, the Amur, Magadan and Sakhalin Oblasts (including the Kuril Islands), the Jewish Autonomous Oblast and the Chukotka Autonomous Oblast. It has less than 6.3 million residents (4.3% of Russia's population), being one of the least densely populated territories of the Russian Federation.

The region constitutes a relatively small share of the Russian economy in contrast to its resource and production potential. Productivity and volume of innovative production are below the Russian average. Capital investment levels and real household net disposable income of the population are also subpar. Over 90% of the investments are directed towards the oil and gas production sector. The Far Eastern Federal District is ranked last but one among all the Russian federal districts as regards the value of subsidies from the federal budget (see Table 1).

The regions which represent the greatest share of Gross Regional Product (GRP) of the Russian Far East are: Sakhalin Oblast (22%), Primorsky Krai (20%), Yakutia (19%) and Khabarovsk Krai (18%). GRP in the remaining federal regions is below the Russian average (less than 40% of the Russian average in the Republic of Buryatia and less than 50% in Zabaykalsky Krai). Yakutia and Sakhalin Oblast are the two federal subjects responsible for over 50% of investments in the region. More than half of the macroregion's export potential is generated by Sakhalin Oblast. Owing to its rapid development, Sakhalin Oblast has become the only federal subject in the Far East not to use subsidies from the federal budget.

Table 1. The level of budget investments from the federal budget to individual federal districts

	2010–2015		2015/2010 (in %)
	in billions of roubles	position among the federal districts	
Central	18,094.1	1	126.6
Ural	12,417.1	2	121.7
Volga	12,286.1	3	119.4
North-West	8,211.7	4	90.2

	2010–2015		2015/2010 (in %)
	in billions of roubles	position among the federal districts	
Siberia	7,965.4	5	101.0
South	7,309.5	6	98.4
Far East	5,358.2	7	83.7
North Caucasus	2,511.9	8	121.4

Source: Экономическая конъюнктура в Дальневосточном федеральном округе в 2015 г., *Пространственная экономика*, № 2, 2016, page 129.

The collapse of the USSR severely affected the economic development of the region. Factories and enterprises which had lost subsidies and state orders began limiting production or winding up within the first five years after the collapse of the USSR. Output fell in practically all sectors of the economy. The production level fell most of all in light industry (22 times), construction (9.6 times), chemicals (6.4 times), machine-building (6.2 times), forestry (4.5 times) and the metallurgical industry (2.8 times)¹. The export share of machines and equipment fell from 30% in the early 1990s to 2.3% in 2012. In turn, the export share of hydrocarbons, fuels, metals and unprocessed wood increased to 85–90%. Residents, especially young people, deprived of jobs and incomes, began emigrating on a massive scale, mainly to the central regions of Russia (the number of people employed in industry decreased by 64%).

Before the collapse of the USSR, the **defence sector** used to be the region's key production area. 34 large machine-building factories operated in the Far East in the 1980s, selling their products mainly to the defence sector: aircraft and helicopters, submarines (including nuclear), warships, sea-to-sea and sea-to-air missiles, radio contact equipment and many other devices. Shipyards and repair yards working for the needs of the defence sector were concentrated in the Amur Valley (the factories in Sretensk, Blagoveshchensk, Khabarovsk, Komsomolsk-on-Amur and Nikolayevsk-on-Amur) and in Vladivostok.

Ferrous (black) and non-ferrous (coloured) metallurgy (26%) of industrial production, concentrated in Yakutia and Khabarovsk, Amur and Magadan Oblasts and in the Jewish Autonomous Oblast, had the largest share of output of the

¹ А. В. Хорошавин, В. К. Заусаев, Дальний Восток России: как жить и хозяйствовать?, Khabarovsk 2012.

Russian Far East towards the end of the 1980s. Irkutsk Oblast is the centre of non-ferrous metallurgy, where almost 40% of Russian aluminium is produced. In addition to this, gold, silver, diamonds and numerous ores and rare-earth elements are mined and processed there. The macroregion also extracts oil (4% of Russia's output) and natural gas (over 4%), diamonds (95% of Russia's output: Yakutia), gold (2/3 of Russia's output: Yakutia, Magadan Oblast and Chukotka Autonomous Oblast), coal (hard, brown and coking), silver, platinum, zinc and lead (Khabarovsk and Primorsky Krai), tin, tungsten and other resources.

As a result of the so called 'voucher privatisation' in the 1990s, the state-owned property was taken over by local elites and in many cases by local criminal groups. **The timber industry** and fishing were among the sectors which turned into a 'grey economy'. Wood processing (boards, plywood, cardboard, paper), which used to have a 10% share in the Far East's production, became unprofitable without state subsidies, and tax revenues fell to one seventh of their previous levels. Many illegal sawmills emerged, employing unregistered migrants and exporting illegally obtained timber, mainly to China. **The situation in the fishing industry**, where production used to flourish in the Soviet era owing to state subsidies, was similar. The fish caught was processed in fish processing plants or directly onboard of the trawlers and sold on the domestic market². Most fish processing plants went bankrupt in the 1990s, and fish caught from privatised trawlers was supplied directly to Korean, Chinese and Japanese recipients.

The region's GRP figures, investment levels and residents' real disposable money income continued to decline. Agriculture and the food industry also found themselves mired in a deep slump in the absence of state subsidies. Imports from China and other Asian countries turned out to be cheaper than maintaining and developing domestic agricultural production.

The Far East also has significant mineral resources which are located in geologically difficult to access territories extending over various climate zones. Many of the deposits have not been developed as yet (for more information, see part II). The region is also rich in platinum (90% of Russia's resources), diamonds (80%), nickel (79%), copper (79%), gold (75%), uranium (50%), iron ores (18%) and rare earth elements (25%) and many other mineral resources.

² Fish processing centres were concentrated in the Far Eastern seaports: Vladivostok, Nakhodka, Korsakov, Nevelsk, Kholmsk, Yuzhno-Kurilsk and Petropavlovsk-Kamchatsky.

Ample **water resources** are located in the Russian Far East and the part of Eastern Siberia adjacent to it, which satisfy 13.5% of the country's energy needs and are among the largest sources of potable water in Russia (Lake Baikal and the Lena and Amur rivers). The seas surrounding the region are rich in fish and sea products – the estimated resources are 26 million tonnes. Especially valuable resources are salmonids (around 450,000 tonnes are fished annually) and red caviar (16,000 – 17,000 tonnes annually).

The region has **700 million hectares of arable land**, only 1–1.5% of which is used in agriculture, mainly in the south. It also has rich forest resources, estimated at 90.5 million m³ (45% of Russia's resources) which are relatively untapped.

2. The Russian Far East: foreign trade

Foreign trade is playing an increasingly important role in the region's economy, and its potential is much higher than that of trade between the eastern regions and the rest of Russia. The Far Eastern regions which generally have the greatest share of inter-regional trade are: Sakhalin Oblast (43,9%) and Primorsky Krai (22%), and also Yakutia (18,7%) and Khabarovsk Krai (8%)³.

The key exports are: oil and gas (49.1%), fish products (12.6%), timber (4.9%) and metals (1.6%). The goods predominant in imports include machinery and means of transport (52.6%) and light industry products and foodstuffs. The Far East's foreign trade volume in 2016 reached US\$24.4 billion, which means that it fell by around 1/3 as compared to 2014. While trade volume was growing steadily between 2010 and 2014, from US\$26.2 billion in 2010 to US\$38.9 billion in 2014⁴.

As regards the share of individual federal subjects in the Far East's foreign trade, Sakhalin Oblast, which accounts for 48% of the trade, is of key significance. The second most important key trade partner is Primorsky Krai (less than 30%). A detailed specification is provided in Table 2.

³ Data for 2016.

⁴ Экономическая конъюнктура в Дальневосточном федеральном округе в 2014 г., *Пространственная экономика*, № 2, 2017, page 163.

Table 2. The share of individual regions in the Russian Far East's foreign trade (in %)

	2013			2014			2015			2016		
	export	import	trade	export	import	trade	export	import	trade	export	import	trade
Amur Oblast	1.6	3.9	2.3	1.3	3.8	2.0	2.0	2.9	2.5	1.8	2.9	2.1
Jewish Autonomous Oblast	0.1	0.7	0.3	0.1	0.7	0.2	0.2	0.7	0.3	0.2	0.5	0.3
Kamchatka Krai	2.2	0.8	1.8	1.8	0.8	1.6	2.7	1.1	2.3	3.1	1.5	2.7
Magadan Oblast	1.1	3.8	1.9	1.1	1.1	1.1	0.7	0.8	1.4	2.1	0.8	1.8
Primorsky Krai	11.9	70.4	29.4	13.9	71.8	29.5	13.3	62.9	23.9	11.7	55.1	22.0
Yakutia	16.8	1.4	12.2	17.7	0.7	13.1	18.3	3.2	14.9	24.0	1.7	18.7
Sakhalin Oblast	60.7	10	45.4	58.6	12.4	46.2	56.8	19.1	48.0	48.3	29.5	43.9
Khabarovsk Krai	5.4	7.6	6	5	7.6	5.7	5.6	8.1	6.1	8.3	7.2	8.0
Chukotka Autonomous Oblast	0.3	1.4	0.7	0.5	1.2	0.7	0.5	1.2	0.6	0.5	0.9	0.6

Source: Экономическая конъюнктура в Дальневосточном федеральном округе в 2015 г., *Пространственная экономика*, № 3, 2016, page 158; Экономическая конъюнктура в Дальневосточном федеральном округе в 2016 г., *Пространственная экономика*, № 2, 2016, page 164; http://dvtu.customs.ru/index.php?option=com_content&view=article&id=18715:-4-2015-&catid=63:stat-vnesh-torg-cat&Itemid=282/

Asian countries have the largest share of trade with the Russian Far East at over 80%, the key partners being South Korea, Japan and China. Trade with European countries is marginal; the European Union's share of the macroregion's trade is only 10%. A detailed specification is provided in Table 3.

Table 3. The key trade partners of the Russian Far East (in %)

	2013			2014			2015			2016		
	export	import	trade	export	import	trade	export	import	trade	export	import	trade
Japan	32.6	14.4	27.1	29.7	16.9	26.3	32	12.6	27.8	25.7	7.3	21.3
South Korea	30.1	12.1	24.7	32	10.6	26.2	29.1	7.8	24.4	26.2	11.0	22.6
China	19.4	46.8	27.7	19	45	26	19	43.8	24.5	20.7	39.4	25.1
Other	17.9	26.7	20.5	19.3	27.5	21.5	19.9	35.8	23.3	27.4	42.38	8.4

Source: Экономическая конъюнктура в Дальневосточном федеральном округе в 2014 г., *Пространственная экономика*, № 2, 2015, page 159; Экономическая конъюнктура в Дальневосточном федеральном округе в 2015 г., *Пространственная экономика*, № 3, 2016, page 152; Экономическая конъюнктура в Дальневосточном федеральном округе в 2016 г., *Пространственная экономика*, № 2, 2017, page 166.

The main trade partners of Sakhalin Oblast are traditionally Japan (43.4% of total trade) and South Korea (40.2% of total trade). Japan is the key recipient of liquefied natural gas exported from Sakhalin, while South Korea buys mainly crude oil and coal.

The main trade partner for Primorsky Krai is China – 51% of total trade. In the case of Yakutia, the most important partner is Belgium (55% of total trade) – Yakutian diamonds are exported to Belgian polishing plants. Yakutia's other major trade partners are India, China and Israel, considering exports of precious metals and stones. In the case of Khabarovsk Krai and the Jewish Autonomous Oblast, the geographical structure of foreign trade is not really diversified – 84% and 94.5% of their production, respectively, is sold to the Chinese market. Khabarovsk Krai exports mainly timber and related products, and the Jewish Autonomous Oblast exports timber and soy. In the case of Amur Oblast the most important trade partner is China, and the key exports are metal ores and timber. Magadan Oblast does most of its trade with South Korea (79.1% export share), exporting mainly mineral products, fish and other food, and also gold and silver. Fish products are the main exports in the case of Kamchatka Krai and Chukotka Autonomous Oblast – 97% and 85% export share, respectively, and the key trade partners are South Korea, China, Japan and the USA⁵.

⁵ Деловой портрет Дальнего Востока, <http://www.eastrussia.ru/material/delovoy-portret-dalnego-vostoka/>

3. The evolution of the Russian Far East development concept

An analysis of the Soviet/Russian government's policy towards the Russian Far East shows that three main strategic approaches can be identified. Firstly, considering its geostrategic location, the region has been viewed as an area of great importance for the development of infrastructure and the defence industry. Secondly, the fact that the Far East is geographically remote from the centre of the country has entailed the need to launch initiatives aimed at building economic ties with the remaining Russian territory. Thirdly, the identified resource potential of the region began to be perceived as an opportunity for building durable economic relations with neighbouring countries, and thus using this as an impetus for the region's economic development.

3.1. The Soviet period

The so-called '**autonomisation strategy**' which envisaged that the region's own funds and resources would be the main driving engine of the region's development, given the difficult situation in the central part of the Soviet Union, was implemented in the Far East in the period immediately following the revolution in 1917 and in the 1920s. The regional government thus focused on implementing the industrialisation programme, concentrating its efforts mainly on the development of such branches of industry as timber processing, fish processing and gold and coal mining. Towards the end of the 1920s, the Soviet government began gradually shifting towards the policy of regaining control of the region, making actions taken in the region subordinate to the strategy of the Soviet centre. The consequences of this included intensifying the region's exploitation and increasing the level of its subsidies from the central budget by raising wages, offering subsidies to the companies which were partly allocated for by paying high tariffs and energy expenses.

A qualitative change took place in the early 1960s, when the Soviet government decided to partly redirect regional production to the Eastern Asian markets. Thus the production model operating so far – which was principally adapted only for the military's needs – began gradually changing. Establishing co-operation with Japan was expected to be a means of boosting development of civilian production; the co-operation initiated in the mid 1960s concerned timber processing.

Although regional subsidies for defence purposes originally began increasing due to the growing military threat from China from the late 1960s, serious cuts

ultimately had to be made in these subsidies due to the increasingly difficult economic situation, especially in the late 1970s – early 1980s. Attempts were made to compensate for the weakening state support via a renewed openness to intensifying trade with the Eastern Asian countries⁶. However, the uncompetitiveness of Soviet production on the one hand and the deteriorating macroeconomic situation of the USSR on the other turned out to be serious barriers to this.

3.2. The 1990s

After the collapse of the Soviet Union, the new Russian government principally did not take any action that would result in a major improvement of the region's economic situation. Since the state had in fact given up subsidising unprofitable regional production, even in the case of the defence industry, an attempt was made to reorient trade to external markets. However, none of the anticipated outlets for uncompetitive Russian production were found and, as a consequence, this led to a gradual deindustrialisation of the region. The difficult macroeconomic situation in Russia, which reached its peak during the financial and economic crisis in 1998, forced the region to rely on its own resources.

3.3. The rule of Vladimir Putin

The real significance of the Russian Far East in Moscow's policy began to grow as Vladimir Putin took power. The new Russian president was the first to formulate the proposal of 'advanced' development of the Far East. However, this was not so much a consequence of a change in the federal government's policy towards the regions but rather an outcome of the new geopolitical strategy being developed by the Kremlin, an important element of which was re-establishing co-operation with Eastern Asian countries. Using the potential of the fuel and energy sector was a key means to achieve this goal. Another important factor was the significant improvement of the economic situation in Russia, itself resulting above all from growing revenues generated by exports of oil and gas.

Significant (as compared to the 1990s) financial support, offered both from budget funds and by the most important state-owned companies, began to be provided in order to implement the announced priorities. Funds were invested

⁶ А. А. Кокосин, Вопросы долгосрочного развития Восточной Сибири и российского Дальнего Востока в контексте глобальной политической и экономической динамики, Moscow 2012, pages 23-24.

mainly in the development of transport infrastructure (including oil and gas transport infrastructure) and the development of raw material deposits. Pavel Minakir branded this strategy as a concept of cross-border raw material transit, the main intended goal of which was to enable the state to export oil and gas to external markets⁷.

One proof of Moscow's increasing interest in the region is the fact that three development programmes covering the Russian Far East were adopted between 2000 and 2015: one in 2002, one in 2007 and one in 2013.

A characteristic feature of the programme adopted in 2007 (covering the period between 2008 and 2013) was the fact that the central government took a strategic decision to increase the level of federal investments in the region. In fact, the investments were made by state-owned corporations, and the projects initiated concerned only infrastructure development. Thus, the intention of the government in Moscow was to transfer engagement in the region to state-owned and private corporations. Their potential incomes from the sale of oil and gas on the increasingly receptive Asian markets are expected to guarantee a constant presence and economic engagement in the regions.

The programme for 2008–2013 was successful in terms of transport infrastructure development. Some ports were modernised (Vanino, Zarubino and Vostochny). Since the projects were beneficial for the corporations themselves, the state did not have to offer any special financial support apart from backing them politically; at the same time, no initiatives were taken that would be aimed directly at regional development of the Russian Far East, understood as supporting other branches of the economy in addition to the energy and transport sectors.

In 2009, the government adopted the Strategy for Socio-Economic Development of the Far East and the Baikal Region to 2025⁸. Most of its assumptions have not been implemented as of yet due to the government's failure to allocate sufficient funds. In many cases this was the result of the government's concerns that the budget funds would not be used effectively, as had been the case with many previous projects and that the local government elites would be the beneficiaries of the subsidies provided.

⁷ П. А. Минакир, О концепции долгосрочного развития экономики макрорегиона Дальний Восток, *Пространственная экономика*, №1, page 20.

⁸ Russian government's regulation of 28 December 2009 no. 2094-r.

In 2009, Viktor Ishayev, the then presidential plenipotentiary envoy in the Far Eastern Federal District of Russia, pointed out that in order to boost development of the Far East it was necessary to significantly increase state investments (develop the market driven by state demand. This in fact meant returning to one of the concepts implemented in the Soviet era, which was based on the assumption that if the state was interested in achieving certain goals, it had to provide adequate funds for this.

The Russian government wanted the Asia-Pacific Economic Co-operation (APEC) summit, held in September 2012 in Vladivostok, to become an epoch-making moment in the contemporary history of the Far East. The Kremlin's intention was to demonstrate interest in deepening Russian activity in Eastern Asia and enhancing political and economic co-operation with the countries in the region. It turned out that hosting the summit consumed an enormous sum of money – the state spent around US\$20 billion on this event, and the allocated funds were spent predominantly on the construction of bridges and roads and airport modernisation⁹. However, the summit had very limited economic and political consequences, including those in the context of regional development of the Far East, notwithstanding the infrastructure built in Vladivostok (including a new airport with an access road to the city, bridges and a new complex of buildings of the Far Eastern Federal University).

As the Eastern direction began gaining significance in Russian government policy (the 'turn to the East') in 2013, President Putin in his address to the Federal Assembly (December 2012) informed that the development of the Far East and Eastern Siberia would be Russia's national priority in the 21st century¹⁰. Then it was decided to prepare another strategy and programme for the region's socio-economic development, and the newly established Ministry for the Development of the Russian Far East was placed in charge of this¹¹.

The first effect of the new ministry's work was the Programme of Socio-Economic Development of the Far East and Baikal Region adopted by the government in March 2013. The programme provided for reconstruction and

⁹ АТЭС-2012: навстречу саммиту в авральном режиме, <http://newsland.com/user/4296757178/content/ates-2012-navstrechu-sammitu-v-avralnom-rezhime/4383375>

¹⁰ Путин: развитие Сибири и Дальнего Востока - приоритет 21 века, http://www.topnews24.ru/news/headlines_krasnoyarsk/70799-putin-razvitie-sibiri-i-dalnego-vostoka-prioritet-21-veka.html

¹¹ The new ministry was established on 21 May 2012.

modernisation of most of the economic sectors which had been neglected for decades, and its estimated value was 10.6 trillion roubles, i.e. around US\$33.3 billion according to the then exchange rate (including 3.8 trillion roubles, i.e. around US\$11.9 billion, from the federal budget). The financial assumptions adopted as part of the programme turned out to be completely unrealistic, given the deteriorating state budget situation. This was the main reason for the dismissal of the then Minister for the Development of the Russian Far East, Viktor Ishayev¹². The programme prepared by Ishayev was not really innovative, and its pillars were large infrastructural projects, mainly in the transport sector, which were intended to provide a stimulus to region's development.

The new minister, Aleksandr Galushka, and the presidential plenipotentiary envoy in the Far Eastern Federal District, Yury Trutnev, presented their own concept for the region's development. The programme envisaged in the concept did not differ much from the previous one – the priority goals included developing production meant for export and investments in the development of transport infrastructure and the energy sector. What was excluded from the programme were the expensive sectoral projects present in the previous agenda and expenses on developing the healthcare system, education and social welfare. Furthermore, it was decided to finance part of the strategic infrastructural investments from the special federal programme 'Development of the Transport System'. This concerned such projects as BAM (Baikal-Amur Mainline) and Transsib (for more information, see part II). Thus, the main consequence of the programme's amendment was – as anticipated by Moscow – significant reduction of the financial assumptions (from initially planned 3.8 trillion roubles from the federal budget to 346 billion roubles). The modified version of the programme was adopted by the government in April 2014.

Two federal programmes became binding, Economic and Social Development of the Russian Far East and the Baikal Region to 2018¹³ and Socio-Economic Development of the Kuril Islands in 2007–2015¹⁴, the implementation of which was to

¹² Viktor Ishayev performed the function of the special presidential plenipotentiary envoy in the Far Eastern Federal District from 30 April 2009 to 21 May 2012, and he served as the minister for development of the Russian Far East from 21 May 2012 to 31 August 2013.

¹³ Постановление от 15 апреля 2014 г. № 308 Об утверждении государственной программы Российской Федерации «Социально-экономическое развитие Дальнего Востока и Байкальского региона», <http://minvostokrazvitia.ru/upload/iblock/6ed/gp34.pdf>

¹⁴ Федеральная целевая программа «Социально-экономическое развитие курильских островов (Сахалинская область) на период до 2025 года», <http://minvostokrazvitia.ru/upload/iblock/25f/KO2025.pdf>

be coordinated by the State Commission for the Socio-Economic Development of the Far East, the Republic of Buryatia, the Trans-Baikal Territory and the Irkutsk Region. The commission was chaired by Prime Minister Dmitry Medvedev, and its members included heads of the largest state-owned companies and banks, representatives of ministries, governors and representatives of the State Duma and the Federation Council¹⁵. The implementation of the eight-year programme covering the Kuril Islands has had tangible effects only as regards infrastructure and the social sector: modernisation of the water supply and heat distribution networks, and bringing into operation an airport, a geothermal station and a hospital. Unfortunately, the implemented projects were not aimed at developing the region's economy. The main reasons for the lack of pro-development actions were the undersize budget (628.3 million roubles), which was much smaller than the one envisaged under the new programme for the development of the Kuril Islands in 2016–2025 (70 billion roubles) and ineffective governance by the then government of Sakhalin Oblast (in 2007–2015, the oblast was governed by Aleksandr Khoroshavin, who was arrested in March 2015 on charges of corruption)¹⁶.

3.4. The Territories of Advanced Development

The Russian government's policy and the concepts, strategies and programmes adopted before - regardless of the declared intention to ensure comprehensive development of the region -were in fact targeted at continuing the development of the region as a resource base for fossil fuels

The concept of creating so-called 'Territories of Advanced Development' (**Территории опережающего развития; TOR**) in the Russian Far East, with preferential conditions for doing business where industrial production will be concentrated, fits in with this logic.

In order to boost and more efficiently utilise the resource potential of the Russian Far East, and to modernise and develop the processing sector, it is necessary to make costly investments for which there have been no sufficient funds

¹⁵ Состав Правительственной комиссии по вопросам социально-экономического развития Дальнего Востока и Байкальского региона в редакции распоряжения от 10 декабря 2015 года №2517-р, <http://government.ru/info/21015/>

¹⁶ Курилы защитят новой федеральной программой, <http://politrussia.com/world/razvitiie-dalnikh-rubezhey-440/>

for many years¹⁷. The greater part of tax revenues from fossil fuels extraction, processing and export goes to the federal budget, while regional budgets receive only a small fraction of the revenues. Furthermore, many large corporations operating in the Russian Far East are registered in Moscow or Saint Petersburg, and pay taxes in these cities. This has led to the Far East's increasing reliance on the influx of investments financed from the federal budget and also on the influx of foreign capital. The extremely hard geological and climatic conditions and the large distances generate high costs (high capital intensity) of extraction and transport of the fossil fuels to the distant outlets. Investors' activity in the region is only possible owing to tax relief and other financial incentives offered that allow them to compensate for the high costs of doing business in the Russian Far East.

The Territories of Advanced Development were established under the act signed by President Putin in December 2014 in response to investors' expectations. Companies operating in the TORs will benefit from: the preferential taxation system, including an insurance rate of 7.6% instead of 30% for the first ten years; a five-year 'tax holiday' (income tax, real estate tax and land tax) which does not cover the mining tax in the case of oil and gas field operation; and the possibility to get a VAT rebate as part of a simplified and accelerated procedure and a relief in the tax on extraction of mineral resources. It is estimated that the preferential financial conditions will attract in the coming ten years foreign investments worth 1 trillion roubles (i.e. around US\$16.2 billion according to the exchange rate applicable in 2016). Seventeen Territories of Advanced Development have been established so far in the Far East: four in Primorsky Krai, three in Khabarovsk Krai, three in Amur Oblast, two in Sakhalin Oblast, two in Yakutia, one in Chukotka Autonomous Oblast, one in Jewish Autonomous Oblast and one in Kamchatka Krai. A detailed specification is provided in Table 4.

¹⁷ The level of depreciation of equipment used in diamond mining is 41%, in the case of hydrocarbons extraction it is 49%, and in the timber industry it stands at 55%. The situation in the fuel and energy sector is especially difficult. Without state subsidies the sector has no prospects for any major development.

Table 4. List of Territories of Advanced Development established in the Russian Far East¹⁸ (according to the creation dates)

TOR name	Creation date	Location	Area of operation
Khabarovsk	25 June 2015	Khabarovsk Krai	Transport and logistics, metallurgy; planned investments using private funds: 30 billion roubles; planned federal budget expenses: 1.258 billion roubles; planned expenses from the regional budget and of extra-budgetary funds: 1.103 billion roubles; around 3,000 jobs are expected to be created
Komsomolsk	25 June 2015	Khabarovsk Krai	Production of parts for the aviation industry; planned investments using private funds: 15 billion roubles; planned federal budget expenses: 902.6 million roubles; planned expenses from the regional budget and of extra-budgetary funds: 329.64 million roubles; around 3,000 jobs are expected to be created
Nadezhdinskaya	25 June 2015	Primorsky Krai	Logistic and transport services; planned investments using private funds: 6.7 billion roubles; planned federal budget expenses: 1.986 billion roubles; planned expenses from the regional budget and of extra-budgetary funds: 1.986 billion roubles; around 1,600 jobs are expected to be created
Mikhailovskaya	21 August 2015	Primorsky Krai	Agriculture; planned private investments: 39 billion roubles; planned federal budget expenses: 2.219 billion roubles; planned expenses from the regional budget and of extra-budgetary funds: 2.219 billion roubles; around 2,400 jobs are expected to be created
Belogorsk	21 August 2015	Amur Oblast	A soy processing plant and other plants in the food industry; planned private investments: 1.45 billion roubles; planned expenses from the regional budget and of extra-budgetary funds: 46.2 million roubles; around 200 jobs are expected to be created
Priamurskaya	21 August 2015	Amur Oblast	A cement factory; planned investments using private funds: 130 billion roubles; around 1,500 jobs are expected to be created
Kangalassy	21 August 2015	Yakutia	Processing industry (mainly oil and gas); a cement factory; planned private investments: 1.11 billion roubles; planned federal budget expenses: 113.2 million roubles; planned expenses from the regional budget and of extra-budgetary funds: 87 million roubles; around 350 jobs are expected to be created

¹⁸ Four TORs have been established so far outside the Far East: ‘Gukovo’ in Rostov Oblast, ‘Neberezhnye Chelny’ in Tatarstan, ‘Usolye-Sibirskoye’ in Irkutsk Oblast, ‘Sarov’ in the Nizhny Novgorod region. Situation as of 30 April 2017.

TOR name	Creation date	Location	Area of operation
Beringovskiy	21 August 2015	Chukotka Autonomous Oblast	Coal mining; planned investments using private funds: 8 billion roubles; around 450 jobs are expected to be created
Kamchatka	28 August 2015	Kamchatka Krai	A tourist and recreational cluster and a transit port for goods exported via the Northern Sea Route; planned private investments: 28.1 billion roubles; planned federal budget expenses: 5.728 billion roubles; planned expenses from the regional budget: 2.737 billion roubles; around 3,000 jobs are expected to be created
Bolshoy Kamen	28 January 2016	Primorsky Krai	The goal of its establishment is effective development of shipbuilding using the Zvezda complex as a base; planned expenses from the federal budget: 3.152 billion roubles; 5,500 jobs are expected to be created
Yuzhnaya	16 March 2016	Sakhalin Oblast	Agriculture (poultry breeding); planned private investments: 6.3 billion roubles; planned expenses from the regional budget and of extra-budgetary funds: 1.46 billion roubles; 450 jobs are expected to be created
Gornyy Vozdukh	16 March 2016	Sakhalin Oblast	A tourist and recreational complex; planned private investments: 6.1 billion roubles; planned expenses from the regional budget and of extra-budgetary funds: 10.031 billion roubles; 725 jobs are expected to be created
Amuro-Khinganskaya	27 August 2016	Jewish Autonomous Oblast	creation of complex enterprises, including processing enterprises of consumer goods and food industries, hotel and exhibition centers and many others
Yuzhnaya Yakutia	28 December 2016	Yakutia	7 mining, transport and logistics and industrial projects; planned private investments: 24.7 billion roubles; the entire infrastructure will be created at the expense of investors
Neftekhimicheskyy	7 March 2017	Primorsky Krai	Rosneft will be the main investor. It is planning to build a petrochemical plant; the company plans to invest in total around 0.5 trillion roubles
Nikolayevsk	19 April 2017	Khabarovsk Krai	Industrial center for deep processing of aquatic bioresources in the Far East
Svobodnyy	3 June 2017	Amur Oblast	Gazprom and SIBUR will be the main investors. They are planning to build gas processing plants; the two companies plan to invest in total around 1.2 trillion roubles

Source: Территории опережающего развития: 12 особых зон в ДФО, <http://tass.ru/info/2215388>; <http://government.ru/docs/27962/>; http://www.dfo.gov.ru/press/news_DV/1756/; <http://government.ru/docs/25925/>; <http://government.ru/docs/27406/>; <http://static.government.ru/media/files/XB98Ar6or-WvxNg21ZnM8ui27A6LuYkpX.pdf>

The federal government is planning to establish more TORs. Rosneft has made efforts to ensure that preferential financial conditions are provided for the planned refinery near Nakhodka (it will be the main investor as part of a TOR

planned to be established in Primorsky Krai¹⁹) along with United Aircraft Corporation and its subsidiary Sukhoi, whose aircraft plants in Komsomolsk-on-Amur are among the largest manufacturers in the Far East. Other companies interested in the financial incentives are: United Shipbuilding Corporation²⁰ which owns the Amur shipyard; Gazprom, which is planning to build a gas processing plant in Belogorsk (Amur Oblast) jointly with SIBUR (after the Power of Siberia gas pipeline has been built)²¹; Rosnano, which is engaged in the production of composite materials in Yakutia (Basalt project)²². TORs are also expected to cover port infrastructure (the ports of Zarubino, Sovetskaya Gavan and Petropavlovsk-Kamchatsky). The preferential investing conditions applicable in the TORs are also expected to apply to investments in the Kuril Islands²³.

It will be impossible to turn the Far East into a region with a diversified and competitive economy if only budgetary funds are used. The government optimistically assumes that investments of public funds will attract private capital. It is estimated in the programme that each invested rouble of public funds will attract around seven roubles of private investments. The Far East and Baikal Region Development Fund established in 2011 is expected to support the implementation of large investment projects. However, despite its recapitalisation up to the level of 15 billion roubles²⁴, it has not become an effective instrument for financing pro-development initiatives. One of the reasons is that the fund prefers financing projects with a high rate of return and those characterised by a quick return of invested funds, while the infrastructural projects being implemented in the macroregion fail to meet such conditions. At present, a recapitalisation of the fund with taxes on the implementation of infrastructural projects in the Far East is under consideration.

¹⁹ Проект ВНХК «Роснефти» подкрепят статусом территории опережающего развития, <http://www.kommersant.ru/doc/2883809>; Проект ВНХК станет центром ТОР «Нефтехимический» в Приморье, <http://tass.ru/ekonomika/2634881>

²⁰ Взойдет «Звезда». Территорией опережающего развития, <http://vladnews.ru/3880/podrobnosti/vzoidet-zvezda-territoriej-operezhayushhego-razvitiya.html>

²¹ Газоперерабатывающий завод «Газпрома» может получить льготы, <http://www.vedomosti.ru/business/articles/2015/06/17/596652-gazopererativayuschii-zavod-gazproma-mozhet-poluchit-lgoti>

²² Территории опережающего развития: лучше меньше, да лучше?, http://www.eastrussia.ru/material/territorii_operezhayushchego_razvitiya_luchshe_menshe_da_luchshe/

²³ Дмитрий Медведев: Курильские острова могут получить статус ТОР, <http://www.kommersant.ru/doc/2774005>

²⁴ The fund's initial capital was 500 million roubles at the moment of its establishment.

Many experts believe that the TORs will remain another initiative of the regional government (as with the already non-functioning special economic zones in Khabarovsk Krai and Primorsky Krai) whose implementation will not have a palpable impact on the economic development of the Russian Far East. Another reason for scepticism is the proposal to launch TORs without having conducted a comprehensive economic analysis of their effectiveness and usefulness for the region. Furthermore, in order to launch the operation of TORs it is necessary to prepare a costly infrastructure financed from both the federal budget and regional budgets, which may be difficult to achieve given the present difficult situation facing the Russian economy alongside the regions' debts. Only large corporations can benefit from the TORs because they are targeted not at developing local business but towards export-oriented production.

II. ENERGY AND TRANSPORT: ‘THE FLYWHEELS’ OF THE FAR EAST’S DEVELOPMENT

Regardless of the programme goals set forth in the documents which envisage comprehensive development of the Russian Far East, the Russian government’s measures have in practice been concentrated mainly on the energy and transport sectors.

1. The energy sector

1.1. The resource potential

Oil and gas resources are the region’s most strategic wealth. The largest oil fields are located in Yakutia and on the shelf of the Sea of Okhotsk. Estimated total oil resources stand at 10–14 billion tonnes. Natural gas is extracted in three large production centres: Irkutsk, centred around the Kovykta gas field, Yakutia, centred around the Chayanda field, and Sakhalin. The estimated total potential of the gas fields is around 14–15 trillion m³, which accounts for almost 1/3 of total confirmed natural gas resources in Russian territory. In addition to this, the region has rich deposits of brown coal, coking coal and anthracite (mainly in Yakutia, Irkutsk, Amur and Magadan Oblasts and in Primorsky Krai).

According to data for 2015, oil output in the Russian Far East and Eastern Siberia reached almost 63.5 million tonnes, and natural gas output around 40.9 billion m³, i.e. more than envisaged in the Energy Strategy of Russia for the period up to 2030. According to this document, until 2020, oil production in the Far East and Eastern Siberia region is expected to grow to 71–83 million tonnes, and natural gas production to 91–112 billion m³ (a detailed medium- and long-term forecast is provided in Tables 5 and 6).

Table 5. Actual and forecasted oil production (in millions of tonnes)

	Actual production			Production forecasted in the Strategy		
	2005	2008	2015	2015	2020–2022	2030
Eastern Siberia	0.2	0.5	37.1	21–33	41–52	75–69
Far East	4.4	13.8	26.4	23–25	30–31	32–33
Russia total	470.2	487.6	534	486–495	505–525	530–535

Source: Energy Strategy of Russia for the period up to 2030; www.gks.ru

Table 6. Actual and forecasted gas production (in billion m³)

	Actual production			Production forecasted in the Strategy		
	2005	2008	2015	2015	2020-2022	2030
Eastern Siberia	4	4	9.2	9-13	26-55	45-65
Far East (mainly Sakhalin)	3 (2)	9 (7)	31.7	34-40 (31-36)	65-67 (36-37)	85-87 (50-51)
Russia total	641	664	635	685-745	803-837	885-940

Source: Energy Strategy of Russia for the period up to 2030; www.gks.ru

In the case of the **gas sector**, production is expected to grow primarily owing to the operation of the gas fields located in two Eastern Siberian production centres: Irkutsk and Yakutia; their resources are intended to be the base for Russian gas supplies to China. The Irkutsk complex includes the Kovykta field, which contains 1.5 trillion m³ of natural gas; the target annual output is planned to reach 35 billion m³. In turn, the Yakutia complex covers the Chayanda field, containing 1.2 trillion m³ of natural gas, and its target annual output is supposed to reach 25 billion m³. According to the announcement made by the Federal Agency for the Use of Natural Resources in 2010, the operation of the Chayanda field was due to commence in 2016. It was announced in March 2014 that the onset of gas extraction had been postponed: in the case of the Chayanda field until no sooner than 2019 and in the case of the Kovykta field no earlier than 2024. A new stimulus for the development of these gas fields came when Gazprom and CNPC signed a contract covering Russian gas supplies to China in 21 May 2014 in Shanghai. The thirty-year contract stipulates that ultimately 38 billion m³ of gas will be exported annually via the so-called ‘Eastern Route’, i.e. from the Eastern Siberian fields via Blagoveshchensk and Khabarovsk to China²⁵. One day after the contract was signed, the CEO of Gazprom ordered work to be conducted that would enable the commencement of operation of the Chayanda field towards the end of 2018. The promised acceleration of the preparatory work does not guarantee that Gazprom will be able to comply with its contractual obligations in the initial phase of the contract’s term. Given the fact that the initial start of production at the Chayanda field has been rolled back from 2017 to 2019, the production target of 16.1 billion m³ that was supposed to be hit in 2018 will most likely not be attained

²⁵ For more information, see: Sz. Kardaś, The eastern ‘partnership’ of gas. Gazprom and CNPC strike a deal on gas supplies to China, *OSW Commentary*, 16 June 2014, <https://www.osw.waw.pl/en/publikacje/osw-commentary/2014-06-16/eastern-partnership-gas-gazprom-and-cnpc-strike-a-deal-gas>

until at least 2020, with the option that output will not reach 25 billion m³ until 2024 or 2025. In the case of Kovykta, output in the initial period (2024) will be at around 3.4 billion m³, and the level of 30 billion m³ will take 15 years of operation to be reached even in the optimistic scenario. Furthermore, the development of new fields will require large investments: around US\$13.5 billion in the case of Chayanda and around US\$11–15 billion in the case of Kovykta²⁶.

As regards the **oil sector**, the most promising are the Eastern Siberian fields owned by Rosneft. Rosneft, Russia's largest oil company, has confirmed oil resources of 2.36 billion tonnes, and its unconfirmed but promising oil resources are estimated at 1.6 billion tonnes. Even though part of the fields already in operation are located not far away from the ESPO (Eastern Siberia - Pacific Ocean) oil pipeline, most of the fields, especially those which are only planned to be put into operation, are situated quite far from the pipeline: 300–800 km, and some even 1,500 km away from it. Furthermore, given the much more difficult geographical conditions, geological work conducted in the fields is more expensive and takes on average double the time than was the case with the Western Siberian fields²⁷.

Lack of funding is the main barrier causing delays in the field development plans. On the one hand, almost 40% of the total amount of funds allocated by the federal government for geological work goes to Eastern Siberia and the Far East (5.5 billion roubles in 2012; 5.8 billion roubles in 2013, 5.1 billion roubles in 2014 and less than 4 billion roubles in 2015). On the other hand, these funds are insufficient in comparison to what is required and, according to experts' estimates, should be increased by at least 30%. Secondly, low oil prices and the increasing fiscal burden imposed on Russian oil firms has led to a reduction of energy companies' investment budgets and thus will contribute to delays in the development of new fields.

Another potential obstacle to the development of the gas fields - albeit in the long term - is that of sanctions. The imposition of the so-called 'technological sanctions'²⁸ may gravely affect gas extraction projects on the coastal

²⁶ *Ibidem*.

²⁷ Восточный фронт, *Нефтегазовая вертикаль*, 2013, № 20, pages 28-29.

²⁸ It is forbidden under EU regulations to supply to Russia any equipment, technologies and services linked to exploration and development of deep-water, Arctic and shale oil fields. The USA has imposed analogous sanctions on Rosneft, Gazpromneft, Transneft, Gazprom, LUKoil, Novatek and Surgutneftegaz. A ban on imports and exports of weapons and mili-

shelf, especially the Sakhalin shelf. The projects implemented there are 100% dependent on imports of equipment and technologies from Western countries, mainly the USA. One consequence of maintaining the restrictions in this area could be a 5- to 10-year delay in the implementation of these projects, which will make it more difficult to achieve the parameters envisaged in the latest version of the draft version of the Energy Strategy of Russia for the period up to 2035 (an increase in output from the shelf from the present level of 17 million tonnes to 50 million tonnes in 2035)²⁹.

One example of how the sanctions mechanism operates is the imposition of US sanctions on the Yuzhno-Kirinskoye field located in Sakhalin (the decision was announced on 7 August 2015)³⁰. Natural gas extracted from this field was to be used as a raw material base for exports as part of the planned development of the Sakhalin-2 LNG terminal. Gazprom planned to engage the US firm FMC for developing the field (making drills on fields located underwater). The sanctions regime may delay the production launch until 2020 (in 2025–2027, the field was expected to supply around 16 billion m³ of natural gas). Sanction measures were imposed on this field shortly after Gazprom had signed a strategic co-operation agreement with Shell (in June 2015 in Saint Petersburg).

Table 7. Increase in oil reserves (in millions of tonnes)

	2015	2020–2022	2030
Eastern Siberia	165	1200	1200
Russia total	1854	5597	5122

Source: Energy Strategy of Russia for the period up to 2030

Table 8. Increase in gas reserves (in billions m³)

	2015	2020–2022	2030
Eastern Siberia	480	1400	1200
Russia total	4100	5400	6500

Source: Energy Strategy of Russia for the period up to 2030

tary equipment to and from Russia and on supplying dual-use goods and technologies to Russia for civil and military purposes has also been imposed.

²⁹ Минэнерго ожидает роста добычи нефти на шельфе до 50 млн тонн в 2035 г., <http://ria.ru/economy/20150915/1252471672.html#ixzz3uZkQr2k7>

³⁰ This was the first case where sanctions were imposed on an individual Russian project (field).

1.2. The infrastructure

The Far East plays an extremely important role in the context of the key assumptions of Russian energy policy, particularly those concerning the development of infrastructure enabling the diversification of Russian oil and gas export routes.

The ESPO oil pipeline (built in 2007–2012) was the first pipeline project of strategic significance. Its first section, running from Tayshet to Skovorodino, entered operation in 2010 (with an initial capacity of 50 million tonnes). The second section of ESPO-2, connecting Skovorodino and Kozmino, came into operation in December 2012 (initial capacity of 30 million tonnes). Another important section is the branch running from Skovorodino to Mohe in China, since this enables exports of Russian oil to China directly by land. In December 2014, the CEO of Transneft announced an increase in the transport capacity of the ESPO-1 pipeline from 50 to 58 million tonnes.

This oil pipeline is of fundamental significance for Russia because it enables Russian oil exports to Asian markets, especially China, Japan and South Korea. Since the launch of the Far Eastern pipeline, the role played by the Asian route in Russian oil exports has been steadily growing. In 2015, China achieved the status of the primary individual Russian oil importer (in aggregate, taking into account all routes, it imported 41.29 million tonnes of crude oil from Russia). Japan and South Korea have also become important recipients of Russian oil³¹.

However, the present transport capacity is insufficient, considering the Russian companies' (mainly Rosneft's) plans to increase crude oil exports. In 2016, Kozmino port practically reached the limits of its export capacity³². Meanwhile, it is impossible to increase the oil flow capacity of the ESPO branch running to China (Skovorodino–Mohe) due to delays in construction work on the Chinese side³³.

³¹ For more information, see: M. Kaczmariski, Sz. Kardaś, 'The oil friendship': the state of and prospects for Russian-Chinese energy cooperation, *OSW Commentary*, 17 February 2016, <https://www.osw.waw.pl/en/publikacje/osw-commentary/2016-02-17/oil-friendship-state-and-prospects-russian-chinese-energy>

³² The port's present capacity is around 31.5 million tonnes. Rosneft will be forced to launch negotiations to receive additional export quotas granted by Transneft to LUKoil and Surgutneftegaz. Роснефти для поставок в Китай нужен весь объем ВСТО, <http://www.komersant.ru/doc/2655227>

³³ This version has been presented by the Russian side, for example, the CEO of Transneft, Nikolai Tokarev. According to arrangements with CNPC, Rosneft was obliged to increase exports to China in 2015 by 5 million tonnes, and in 2018 up to 30 million tonnes. Initially,

As previously assumed, an increase in the transport capacity of existing infrastructure is expected by 2020: in the case of the Tayshet-Skovorodino section this would take it to 80 million tonnes, and in the case of the Skovorodino-Kozmino section to 50 million tonnes. According to estimates made in February 2014, the cost of such infrastructure investment would reach 172 billion roubles (around US\$3 billion). Although the falling oil prices and the limited opportunities of attracting external capital due to sanctions may to some extent make the implementation of these investment plans more difficult, given the fact that energy co-operation with China is a priority for Russia, and is politically supported by Vladimir Putin, one might presume that any potential financial difficulties will be overcome, and that infrastructural oil projects will be carried through to completion.

The second strategic project, announced in May 2014, is the construction of the Power of Siberia-1 gas pipeline connecting Russian Eastern Siberian fields and the north-eastern provinces of China. The implementation of the project commenced after Gazprom and China's CNPC signed a contract in May 2014³⁴. The new Russian project is extremely expensive. According to initial estimates, the costs of infrastructure construction and the development of the fields to be used as the sources of supplies may reach as high as US\$55 billion. Gazprom, contrary to initial announcements, has been unable to obtain a loan of US\$25 billion from China that had been promised already in 2014 and which might have facilitated the implementation of the investment. The loan of 2 billion euros granted to Gazprom by Bank of China in early March 2016 is only a small part of the total investment costs³⁵.

The new infrastructure, even though it is intended to be used mainly for export purposes, may also play a certain role in the region's gasification programme.

it was planned to increase the transported volume of oil using the Skovorodino-Mohe pipeline (a branch of the ESPO oil pipeline). However, it was impossible to actually increase the volume of oil transported via the Skovorodino-Mohe pipeline, either in 2015 or 2016; the main reason for this was unfinished work on the Chinese side. Furthermore, according to information provided by the CEO of Transneft in December 2016, China will not be ready to receive more oil via the Skovorodino-Mohe pipeline until 2018 (up to the level of 26.5 million tonnes), and the previously agreed capacity of 30 million tonnes will not be achieved until 2019.

³⁴ According to Gazprom's announcement, 500 km of the gas pipeline has already been constructed since the beginning of February 2017. "Газпром" построил 500 км "Силы Сибири", <http://www.vestifinance.ru/articles/81989>

³⁵ «Газпром» получит 2 млрд евро кредита у Bank of China, <http://www.vedomosti.ru/business/articles/2016/03/04/632474-gazprom-kredita-china>

This concerns both the Baikal region (there is a plan to build a branch of Power of Siberia-1, running from Blagoveshchensk to Chita) and Khabarovsk and Primorsky Krai. However, it is unclear whether these plans will ever be put into practice. Forecasts concerning gas consumption in the Far East and Baikal region differ significantly. According to the findings of experts from the magazine *Neftegazovaya Vertikal*, gas consumption in the macroregion in 2020 may reach anywhere between 5 and 38 billion m³³⁶.

An important project which has been carried out is the gas liquefaction plant in Sakhalin Oblast. The gas liquefaction plant launched in 2009 is currently the only LNG export terminal operating in Russia. The total production capacity of its two branches stands at 10 million tonnes (around 14.5 billion m³ of gas). The largest importers of Russian liquefied natural gas are Japan (almost 70% of exports) and South Korea (around 17%). The remaining part is supplied to China, Taiwan and Thailand (a detailed specification is provided in Table 9.

Table 9. Russian LNG exports (in millions of tonnes)

Importer country	2009	2010	2011	2012	2013	2014	2015	2016
Japan	2.84	6.29	7.18	8.31	8.73	8.32	7.78	7.38
South Korea	1.02	3.39	2.82	2.17	1.96	2	2.69	1.92
Kuwait	0.31	0.07	0	0	0	0	0	0
China	0.19	0.38	0.24	0.38	0	0.13	0.19	0.26
Taiwan	0.12	0.51	0.18	0.06	0.06	0.06	0.26	1.29
Thailand	0	0	0.06	0	0	0.06	0	0
India	0.51	0	0	0	0	0	0	0
Total	4.99	10.64	10.48	10.92	10.75	10.57	10.92	10.85

Source: Author's own calculations based on data published annually in the World LNG Report.

Russian firms are planning to build more LNG terminals: Gazprom intends to build a new LNG terminal in Vladivostok (total production capacity of 10 million tonnes). In turn, Rosneft plans to build its own terminal as part of the Sakhalin-1

³⁶ *Нефтегазовая вертикаль*, 2014, № 13–14, page 52.

project (one branch with a production capacity of 5 million tonnes). The difficult financial situation of Russian firms resulting on the one hand from low global oil prices and on the other from the financial and technological sanctions imposed on Russia (due to aggression against Ukraine in 2014) may, however, thwart these plans in the medium term.

2. Transport

The second most promising area (after the energy sector) is the transport sector. Its development and modernisation is one of the key elements in maintaining links with the centre of the federation. Besides, the Far East plays an important role in international transport, especially to such countries as Australia, China, North and South Korea and Japan.

However, the problem is that the transport infrastructure is developed unequally in the Russian Far East. The southern regions and Sakhalin Island have quite well-developed road networks. In contrast, the northern regions practically have no connection with the southern areas and the centre of Russia alike. For this reason, transport network development has become not only a stated goal but also a real priority for the central government, which is interested in intensifying imports of raw materials and goods to Asian and European countries as well as profiting from the transit of cargo from Asia to Europe.

Another challenge the government needs to face is the fact that **the transport system in the Far East is not logistically integrated** (warehouses, sorting centres, transshipment and customs points, etc.). There are many logistic problems with transport hubs, especially those connecting railroads with seaports, and the disparities in their technological equipment are a barrier to increasing the volume of transshipment and the development of international transport.

Rail transport and the Far Eastern ports currently occupy a key role; yet the role of road and air transport is also growing steadily.

2.1. Railroad transport

The Far East's **rail transport** is based on two main lines: the Trans-Siberian Railway (Transsib) and the Baikal-Amur Mainline (BAM). Transsib is a railway line almost 9,300 km-long, connecting Moscow and Vladivostok (the route runs through such cities as Perm, Yekaterinburg, Novosibirsk, Irkutsk, Chita, Birobidzhan and Khabarovsk). In turn, BAM is a railway line around 4,300 km-long

connecting Tayshet, a town in Eastern Siberia, and the Far Eastern port of Vanino and – taking into account the ferry connection – Sovetskaya Gavan in Sakhalin (the precise route of the two railway lines is presented in a map – see Appendix). However, both the present transport capacity and the technical condition of the two railroads prevent the development of bulk cargo (oil, petroleum products, construction materials, timber) and general cargo³⁷.

Chukotka Autonomous Oblast, Kamchatka Krai and Magadan Oblast have no access to railroads at all. The total length of the region's rail network is only 14% that of the Russian rail network as a whole, and its density per 10,000 km² is 3.6 times smaller than the general Russian average.

2.2. Maritime transport

Maritime transport plays a major role in the Russian Far East's economy. 28 sea and fishing ports operate along the 5,600 mile-long coastline, handling 17% of the cargo of all Russian seaports and 95% of the cargo in the Far East. The transshipment volume in the Far Eastern ports in 2015 reached 171 million tonnes, which meant a 8.5 million-ton growth as compared to 2014³⁸. The Far Eastern seaports are used above all to export Russian coal, timber, oil, petroleum products and ores. The predominant imports are grain, sugar, metals, cement, chemical products, machines and equipment. The Far Eastern ports play an especially important role in cabotage transport, mainly from Primorsky Krai to the northern ports of Kamchatka Krai, Magadan Oblast and Sakhalin Oblast, for which this is the only way to receive cargo. The Far East's largest ports are: Vostochny (transshipment of 57 million tonnes), Vanino (26 million tonnes), Nakhodka (21 million tonnes), Vladivostok (15 million tonnes), De-Kastri (8 million tonnes) and Posyet (7 million tonnes), which tranship over 83% of the cargo³⁹. The ports of Primorsky Krai and Vanino in Khabarovsk Krai are connected with Transsib and BAM via which over 90% of the cargo are transported and are the most important transport hubs in the region.

³⁷ Изменения, которые вносятся в постановление Правительства Российской Федерации от 15 апреля 1996 г. № 480, Об утверждении федеральной целевой программы «Экономическое и социальное развитие Дальнего Востока и Забайкалья на период до 2013 года», <http://www.open.minvostokrazvitia.ru/interrogations/22/1555/>
BAM's present transport capacity is 16 million tonnes of cargo. It is planned to be increased to 55 million tonnes in 2020. Transsib's annual capacity is 100 million tonnes of cargo, while the annual demand is at least 120 million tonnes.

³⁸ <http://primamedia.ru>

³⁹ 85% export cargo and 45% import cargo are handled by the Far Eastern seaports.

At the same time, the regularly growing demand for international and cabotage transport means that **the Far Eastern sea ports need to be developed and modernised**. Many of them require increasing capacity (the total transshipment volume of the 28 sea ports in the Far Eastern Federal District is six times lower than that of Shanghai port). Demand for bulk cargo transshipment is growing, especially in the ports handling exports. Due to underinvestment in the ports and their transport infrastructure, their transshipment capacity is utilised to only 60%⁴⁰. The situation may be improved by the act of 13 July 2015, establishing the 'Free Port of Vladivostok'⁴¹ where imported goods will be duty and VAT free, and where tax rebates will apply for five years.

The Northern sea basin including the White Sea, the Barents Sea and the seas of the Arctic Ocean, being part of the Northern Sea Route, is playing an increasing role in maritime transport. The maritime fleet operating in this region ensures supplies to the northernmost territories of the Far East – the Arctic islands. The development of the Northern Sea Route's infrastructure will allow a shortening of the route via which goods are transported from China, Japan and Korea and also from Northern America to Europe by nearly 4,000 km.

River transport is of lesser significance. It is based on the two largest routes: the Lena and Amur Rivers. Seasonality is the factor that limits its significance to the region's economy; this transport route can be used only for 160–180 days a year due to freezing temperatures. Failure to modernise the river fleet and its infrastructure and the high costs of transport and reloading of goods represent additional limitations.

2.3. Road transport

The share of truck transport in the transport of goods and passengers is regularly growing. Road transport plays the most important role in interregional and frontier freight. The most important roads are the federal car routes: 'Amur' (Chita–Skovorodino–Birobidzhan–Khabarovsk – 2097 km), 'Ussuri' (Khabarovsk–Vladivostok – 767 km), 'Vostok' (Khabarovsk–Nakhodka – 824 km), 'Lena' (Bolshoy Never–Yakutsk – 1157 km), 'Kolyma' (Yakutsk–Magadan – 2021 km). The APEC summit held in Vladivostok in 2012 accelerated the development and modernisation of the road network and the improvement of its

⁴⁰ Порты Дальнего Востока, <http://www.realeconomy.ru/221/1480/5419>

⁴¹ Федеральный закон от 13 июля 2015 г. N 212-ФЗ "О свободном порте Владивосток", <https://rg.ru/2015/07/15/fz212-dok.html>

infrastructure (for example, some of the checkpoints on the border with China were developed and modernised). 119 km of roads were built or reconstructed, including the route running from Vladivostok to the international airport and the 'Ussuri' road from Vladivostok to Nakhodka. Three suspension bridges were also built in Vladivostok (the 2.1 km-long bridge over Zolotoy Rog bay; the 3.1 km-long bridge over the strait called Eastern Bosphorus to Russky Island; the 4.3 km-long low-water bridge over the Amur Bay) and roads were built on Russky Island where the meetings as part of the APEC summit were held⁴².

Although demand is growing, the road infrastructure is still **poorly developed**. The average road density in the region is only 5.3 km per 1000 km², while the Russian average is 31.7 km per 1000 km²⁴³. As many as 1400 population centres in the region lack any access to road infrastructure. Almost half of the roads fail to meet technical standards (such as not being covered with asphalt) and do not guarantee safety of the rapidly growing truck transport. On the one hand, both extremely difficult climate conditions and the low population level lie behind the paucity of roads, especially in northern territories. On the other hand, infrastructure modernisation poses a serious challenge, given the intensifying competition from Chinese carriers (three roads and three railroads run through the 4,200 km-long border)⁴⁴.

2.4. Air transport

Air transport plays a major role in transporting passengers and goods both inside the macroregion and to/from the central regions of Russia. It is often the only means of transport, enabling connections with the difficult to access northern territories. It also enables landing on Sakhalin and the Kuril Islands. 107 civilian airports are currently present in the Russian Far East, yet only 52 of them have runways meeting international standards and the remaining have only dirt runways at their disposal⁴⁵. Only 67% of the airports have

⁴² *Транспорт России*, № 10(817), 6 March 2014.

⁴³ <https://rg.ru/2010/10/18/set.html>

⁴⁴ At present, goods are transported under a bilateral agreement setting the number of annually issued transport licences. Their number is increasing every year. In 2013, Russian carriers received 61,260 licences, and Chinese carriers received 60,450 licences. The Chinese party, fearing competition from Russian carriers, allows Russian trucks to enter China only from Russia, not allowing transit from third countries, e.g. Kazakhstan.

⁴⁵ Data provided by the website *Транспорт России*, <http://www.transportrussia.ru>

adequate infrastructure facilitating flight handling, including lights⁴⁶. Most airports need to be developed, modernised and adjusted to the applicable technical standards. The state of the airports is one of the factors which discourages potential investors from engagement in the region.

⁴⁶ The number of passengers at the Far East's largest airport in Khabarovsk is 27 times smaller than at Singapore Airport (1.9 million as compared to 51 million of passengers in 2012).

III. THE MAIN BARRIERS TO THE DEVELOPMENT OF THE RUSSIAN FAR EAST

The government's activity in the Russian Far East, most visible in the strategic energy and transport sectors, has changed Moscow's ambivalent attitude towards the region as seen in the 1990s. Nevertheless, although the region has gained significance on the list of the federal priorities, it does not allow the centre of the federation to fulfil its assumed political goals. Moscow has been unable as yet to generate tangible development activity in the region. As a result, the Far East has not become yet an important instrument for strengthening Moscow's economic influence in Eastern Asia. The expectations of intensifying cross-border economic co-operation in the Russian Far East and attracting major foreign investments to the regions remain unrealised.

The causes of this predicament are above all internal and in some respects are linked to the systemic problems existing across Russia, while in other respects are of a specifically local nature.

1. The lack of a consistent development concept and the ineffective governance system

One of the major barriers halting development is the lack of a consistent concept for economic development of the Russian state. The consequences of this include the lack of well-thought-out regional strategies, including those concerning the Far East. Proof of this includes both the multitude of programme documents adopted at the federal level (strategies, concepts and programmes) and the inconsistency in the implementation thereof. Most strategic decisions concerning the Russian economy are strictly subordinate to decisions of a purely political nature as regards both domestic and political issues. The best example illustrating this is in the consequences of Russia's aggressive policy towards Ukraine, resulting in sectoral sanctions imposed by the West on Moscow and corresponding Russian counter-sanctions. Their adverse effect on trade has also been visible in the case of the Far East; the value of imports to the Far Eastern Federal District was nearly halved – it fell from US\$10.5 billion in 2014 to US\$5.7 billion in 2015 (US\$5.8 billion in 2016).

Another example of the lack of consistency on the level of stated versus actually conducted economic policy of the state is the postulate that it is necessary to diversify the Russian economy and reduce its reliance on the fuel and energy sector. This does not correspond to the actual measures taken, either at the federal or

regional levels. The budget incomes are still based predominantly on the revenues from the fuel and energy sector; on the other hand, the state treats investments in the energy sector as a priority. One example of this is the expensive gas pipeline projects implemented in Europe (Nord Stream 2 and Turkish Stream) and Asia (Power of Siberia-1). Another example of the inconsistent approach is provided by tariff policy. The high tariffs (on transport, energy and other) have led to the share of transport costs in the value of oil and gas transported reaching 50%; the share of transport costs is also high in the case of metallurgical products.

The increasingly ineffective governance system on both the federal and regional level is another major barrier. On the one hand, the decision-making process has been centralised during the presidency of Vladimir Putin. On the other hand, numerous structures have been created in the case of the policy adopted towards the Far East, without clearly distributing the competences. For example, the entities tasked with planning and implementation of projects concerning the Far East in 2012–2014 were: the Ministry for the Development of the Russian Far East, the special plenipotentiary envoy of the president of the Russian Federation in the Far Eastern Federal District, the Ministry of Regional Development of the Russian Federation (shut down in September 2014) and a number of smaller agencies and funds.

The system for redistributing the funds earned by the economically strategic sectors is also ineffective and unrewarding from the regional perspective. Unprocessed raw materials are exported directly from the mining site to recipients in Asian countries. The resulting funds received accrue mainly to the centre of the federation, while only a small portion of them remains in the region. Consequently, the regions which are suppliers of raw materials have to rely on subsidies from the federal budget.

The ineffective governance system also adversely affects projects of strategic significance. One example is the construction of the Vostochny spaceport in Amur Oblast, which, according to President Putin's order, was to be put into operation towards the end of 2015. This investment is of strategic significance for Russia because it would mean that Russia is no longer dependent on the Baikonur spaceport in Kazakhstan. As revealed by an audit, the cost estimates of the work have been inflated and some of the funds have been misappropriated. It has been impossible to supply part of the equipment ordered under contracts due to Western sanctions. Furthermore, construction work has also been delayed due to financial problems affecting many subcontractors, caused by difficulty in obtaining funding and high loan costs.

2. Staffing problems in the Russian Far East

The small number of inhabitants, which has been declining for many years, represents one of the most serious barriers to the development of the Far East. Its residents, especially young and educated ones, leave the macroregion for the central regions of Russia in search of better living and work conditions. The main reasons for the continuing migration of its citizens for many years have been the loss of many jobs following the collapse of the USSR and the closure of numerous production facilities. Other factors encouraging migration are: harsh climate conditions, higher living costs compared to other regions and underfunded healthcare, education and social welfare system. Between 1990 and 2010, one in five residents of the Far East left the region, most of them being young people of productive ages. The largest migration wave (42%) has affected the northern regions of the Far East (69% of residents have left Chukotka Autonomous Oblast and 55% have emigrated from Magadan Oblast)⁴⁷. The low birth rate and the high mortality rate (higher than Russian average) are further contributors to the difficult demographic situation in the macroregion⁴⁸.

At the same time, it is worth noting that the downward demographic trend has abated over the past few years. The population in the Far East declined on average by 0.2–0.4% in 2011–2015. One positive factor is that the number of births exceeds the number of deaths: by 7,400 people in 2013, by 9,300 people in 2014, by 8,100 people in 2015 and by 5,077 in 2016. The population growth rate has increased over the past decade from 11.6 per 1 thousand in 2005 to 14.0 per thousand in 2014 (13.9 per thousand in 2015 and 13.3 per thousand in 2016).

On the one hand, an upward trend has been observed in the migration balance, indicating that the number of residents emigrating from the region has been steadily falling (detailed data are provided in Table 10). On the other hand, people with low levels of qualifications predominate among the immigrants, and this does not help address the region's acute staffing problems.

⁴⁷ A. В. Хорошавин, В. К. Заусаев, *op. cit.*, page 218.

⁴⁸ In 2011, average life expectancy in the region was 66.4 years (61.6 years in Chukotka Autonomous Oblast and 67.7 years in Yakutia), the Russian average being 69.8 years.

The so-called ‘Far Eastern hectare’ act adopted in 2016 is also expected to help improve the demographic situation⁴⁹. It permits citizens of the Russian Federation⁵⁰ to acquire free of charge one hectare of state-owned land located in the Far Eastern Federal District.

The effects of the act have hitherto been very limited (as of February 2017). Around 40,000 applications were received between 1 June 2016 and 1 February 2017. Only 4,000 of these applications were granted. In turn, since 1 February 2017, when all citizens of the Russian Federation, not just residents of the Far Eastern Federal District, were vested with the right to apply for the land, only 2,500 applications have been submitted. State resources in the district are around 614 million ha of land, almost 90% of which is unused⁵¹.

Table 10. Migrations of people in the Far Eastern Federal District (number of people)

	Immigrants			Emigrants			Balance		
	2014	2015	2016	2014	2015	2016	2014	2015	2016
Yakutia	31 486	36 456	36 715	38 194	41 843	40 868	- 6 708	- 5 387	-4 153
Kamchatka Krai	13 246	13 441	12 561	16 368	14 755	14 366	-3 122	-1 314	-1 805
Primorsky Krai	75 467	77 358	77 058	79 415	80 149	80 267	-3 948	-2 791	-3 209
Khabarovsk Krai	55 847	54 521	57 047	58 382	59 448	58 633	-2 535	-4 927	-1 586
Amur Oblast	29 939	29 566	28 761	31 204	33 181	32 031	-1 265	- 3 675	-3 270

⁴⁹ Федеральный закон от 1 мая 2016 г. N119-ФЗ „Об особенностях предоставления гражданам земельных участков, находящихся в государственной или муниципальной собственности и расположенных на территориях субъектов Российской Федерации, входящих в состав Дальневосточного федерального округа, и о внесении изменений в отдельные законодательные акты Российской Федерации”, <http://dvgektar.ru/threads/tekst-zakona-o-dalnevostochnom-gektare.2/>

⁵⁰ From 1 June 2016 this right was vested only in residents of selected parts of all administrative subjects located within the Far Eastern Federal District; from 1 October 2016 in all citizens of the Russian Federation living in the district, and since 1 February 2017 in all citizens of the Russian Federation, regardless of their place of residence.

⁵¹ Гектар на всю страну, <http://www.kommersant.ru/doc/3207549>; Дальневосточный гектар, <https://rg.ru/2016/06/02/vyzhutovich-poluchateli-am-besplatnogo-gektara-budut-nuzhny-deshevye-kredity.html>

	Immigrants			Emigrants			Balance		
	2014	2015	2016	2014	2015	2016	2014	2015	2016
Magadan Oblast	5 721	5 882	7 883	7 998	7 613	8 622	-2 277	-1 731	-739
Sakhalin Oblast	20 167	21 321	21 971	23 078	22 615	22 458	-2 911	-1 294	-487
Jewish Autonomous Oblast	4 175	4 660	4 754	6 007	6 674	6 356	-1 832	-2 014	-1 603
Chukotka Autonomous Oblast	4 814	4 392	4 280	4 968	4 981	4 796	-154	-589	-516
Far Eastern Federal District	240 862	247 597	251 030	265 614	271 259	268 397	-24 752	-23 662	-17 367

Source: Экономическая конъюнктура в Дальневосточном федеральном округе в 2015 г., *Пространственная экономика*, № 3, 2016, page 145; Экономическая конъюнктура в Дальневосточном федеральном округе в 2016 г., *Пространственная экономика*, № 2, 2017, page 160.

The immigrant issue, and especially the concerns present in Russian public discourse linked to the massive influx of Chinese to the Russian Far East, is a separate problem. Even though serious discrepancies currently exist between official and unofficial data⁵², it seems that the perception of a radical increase in immigration from China (including expatriate workers) is at present more a myth than a genuine threat. On the one hand, the three northern provinces of China bordering the Russian Far East currently have a population of around 100 million, which is viewed as a concern by Moscow, when contrasted with the number of residents of the Far Eastern Federal District (6.3 million people). On the other hand, according to official data collected during the 2010 census in the Far Eastern Federal District, around 8,800 Chinese lived on a permanent basis there, accounting for less than 0.14% of the district's population and around 30% of the total number of Chinese residents of Russia⁵³. According to data from the Ministry of Internal Affairs, around 239,500 Chinese currently

⁵² One example was the statement made by the Minister for Ethnic Policy of the Russian Federation in 2002 that, while the official number of Chinese residents of Russia did not exceed 400,000, according to unofficial estimates, their number might reach even 4 million.

⁵³ Население по национальности и владению русским языком по субъектам Российской Федерации, http://www.gks.ru/free_doc/new_site/perepis2010/croc/Documents/Vol4/pub-04-04.pdf

live in the Russian Federation (as of 5 April 2016), i.e. around 2.4% of the total number of foreigners⁵⁴; according to unofficial data, not more than 500,000 people⁵⁵. In turn, according to experts' estimates, the Chinese population in the Russian Far East may range between 70,000 and 200,000 people (i.e. between 1% and 3% of the total number of residents of the Far Eastern Federal District⁵⁶). Citizens of post-Soviet countries, especially Uzbekistan, Tajikistan and Kyrgyzstan and to a lesser extent of Armenia, Azerbaijan and Ukraine, form an increasing group among the immigrants in the Russian Far East⁵⁷.

There are several reasons behind the relatively low scale of migration among the Chinese population (predominantly a less qualified workforce and small entrepreneurs) to the Russian Far East. Firstly, the living standards and work conditions in the region (in particular, wages) are not really appealing from the point of view of Chinese emigrants, apart from the energy sector, which generates to a limited extent a demand for workers (usually seasonal or linked with the implementation of specific projects⁵⁸). In turn, other branches, especially agriculture, are still very poorly developed. Aside from this, central regions of Russia are the ultimate migration destination for many Chinese who cross the Russian-Chinese border in the Far East. Secondly, another important factor is that the economic development rate is much higher and the unemployment level is relatively low in the north-eastern provinces of China in comparison to the Russian Far East. For example, the unemployment rate is only 4.5% and the GDP growth rate reached 5.7% in 2015 in the Chinese province Heilongjiang (for comparison, GDP in the Far Eastern Federal District fell by 3.7% in 2015). Thirdly, administrative barriers posed by Russian law based on bureaucratized and complicated procedures for border crossing and legalisation of stay do matter to a certain extent. Moreover, the Russian government has

⁵⁴ Т. Н. Журавская, Миграция из стран СНГ в Амурскую область в контексте ситуационной теории, *Пространственная экономика*, № 3, pages 105-106.

⁵⁵ Страшная сказка. Стоит ли бояться захвата Сибири китайцами, <https://lenta.ru/articles/2015/11/24/mythsaboutchinese/>; China's One Belt, One Road Initiative and the sino-Russian Entente. An Interview with Alexander Gabuev, <http://www.nbr.org/research/activity.aspx?id=707>

⁵⁶ Помогут ли китайские и украинские мигранты поднять Дальний Восток?, <http://inosmi.ru/economic/20160216/235429994.html>

⁵⁷ Only around 6.8% of immigrants among the total number of citizens of other countries coming to Russia settle in the Russian Far East (for comparison, over 62% of immigrants settle in the Central and North-Western Federal Districts); Т. Н. Журавская, *op. cit.*, pages 105-106.

⁵⁸ For example, Transneft employs around 1800 Chinese workers as part of the construction of the Eastern Siberia – Pacific Ocean oil pipeline.

been reducing the quotas of work permits granted to foreigners in Russia; for example, in 2017, the limit for the Far Eastern Federal District was reduced by 11.9% (to 6,430 people)⁵⁹. Fourthly, most Chinese citizens who decide to emigrate from their previous place of residence usually settle in other regions of China, especially in the western provinces⁶⁰.

Many factors indicate that the situation is not likely to change within the next decade. It seems unlikely that the economic attractiveness of the Russian Far East will increase. It is also difficult to expect that the attitude of the Russian government – both federal and local – will change in such a manner that it would regard greater openness to migrants from China more as an opportunity rather than as a concern or even threat. The Chinese themselves are also unlikely to become more interested. However, the situation might change in the case of serious ecological problems appearing in China (in particular, the problem with accessibility of water resources or increasing air pollution).

3. The decentralised energy system

Another limitation to the development of the Russian Far East is the **decentralised energy system**, which makes it impossible to send periodical electricity surpluses to other regions which lack sufficient energy resources. Most of this vast area is covered with local transmission networks (the total length of power lines exceeds 105,000 km), and only 25% of the territory is connected to the common Russian transmission network, the United Energy System of Russia (UES of Russia); the energy systems of the Baikal region are part of the common energy system of Siberia, which is connected to the UES of Russia⁶¹. In turn, the power networks of Kamchatka Krai, Magadan Oblast, Chukotka Autonomous Oblast, Sakhalin Oblast and part of Yakutia are not connected to the common energy system. The greatest amount of electricity, generated mainly by hydropower plants, is produced in Irkutsk Oblast (44%). The share of the other regions of the Far East in electricity production is only 9%.

⁵⁹ Дальний Восток примет меньше всего трудовых мигрантов, <http://dv.land/news/9854>

⁶⁰ Перенос страхов: стоит ли опасаться китайских заводов на Дальнем Востоке?, <http://maxpark.com/community/politic/content/5261211>; M. Repnikova, H. Balzer, Chinese migration to Russia: missed opportunities, https://www.wilsoncenter.org/sites/default/files/No3_ChineseMigtoRussia.pdf

⁶¹ OEC Vostok (Amur Oblast, Khabarovsk Krai, Jewish Autonomous Oblast, Primorsky Krai and the southern regions of Yakutia) and OES Sibir are connected with three power lines with a capacity of 200 kW supplying electricity to recipients along the Transsib and BAM railroads but not ensuring power transmission between OEC Sibir and OEC Vostok.

Given the vast distances, low population density and the harsh climate, the local energy sector will be of key importance in the energy system of the Far East. Improving its efficiency is one of the conditions on which potential investments in the region depend, mainly in raw material production and processing, given their cost-efficiency. This would require developing and modernising local power networks, which might lead to reducing energy losses in transmission networks and the costs of connecting new recipients, using local energy sources (including renewable) and employing extra-budgetary funds.

Relatively high tariffs in the power sector also pose a major problem. Traditionally, the tariffs used to be higher in the Far East as compared to the Russian average. Cutting the tariffs for industrial recipients by around 30% in December 2016 was therefore an essential step aimed at improving the situation (for example, the tariff cuts reached 65% in the case of Chukotka Autonomous Oblast, 50% in the case of Yakutia, 46% in the case of Sakhalin Oblast and 34% in the case of Magadan Oblast)⁶².

4. The limited foreign investments

Foreign investment in the Russian Far East is relatively limited and accounts for only 20% of total investment funds. At the same time, the region's share of the total value of foreign investment in Russia has been falling. In 2011, the Far East and Zabaikalsky Region generated around 17% of Russia's foreign investment, in 2012 this share fell to 11.6 % and in 2013 to 9.2%⁶³.

Sakhalin Oblast has been the key federal subject attracting foreign investment. Back in 2005, it accumulated around 96.5% of investment funds. In 2011, its share fell to 70%, and in 2013 to 40%. The main reason has been its attractiveness to firms interested in the implementation of energy projects. One example is Sakhalin-Energy, whose shareholders – in addition to Gazprom (50% plus one share) – are Holland's Royal Dutch Shell (27.5% minus one share) and Japan's Mitsui (12.5% stake) and Mitsubishi (10% stake). The consortium owns a gas liquefaction plant (Sakhalin-2 project), exporting annually around 10 million tonnes of liquefied natural gas (around 14.5 billion m³). Another example is

⁶² Госдума приняла закон о снижении энерготарифов на Дальнем Востоке, <http://www.kommersant.ru/doc/3174709>

⁶³ Деловой портрет Дальнего Востока, <http://www.eastrussia.ru/material/delovoy-portret-dalnego-vostoka/>

the Sakhalin-1 project, whose shareholders are Russia's Rosneft (20% stake), US Exxon Mobil (30%), India's ONGC (20%) and SODECO (30%).

China appears to be the most promising foreign investor - regardless of the concerns sometimes formulated in the Russian public sphere and the relatively small scale of its engagement so far. According to the most recent data provided by Aleksandr Galushka, the Minister for the Development of the Far East, China accounts for 160 billion roubles (around US\$2.8 billion) out of the 1 trillion roubles (around US\$17.3 billion) invested in the Territories of Advanced Development and the Free Port of Vladivostok⁶⁴.

Beijing is interested in developing transport corridors in which the Russian Far East and the Baikal Region will participate. The aforementioned energy projects and also the routes used for transporting goods other than oil and gas are of key significance. The two branches of Primorye corridors: Primorye-1 (Harbin-Vladivostok-Nakhodka) and Primorye-2 (Jilin-Zarubino-Slavyanka) are especially important to Beijing. China's genuine interest has been proven by the fact that Beijing vested local governments of the Chinese frontier provinces with powers to enhance international cross-border co-operation.

Japan may also potentially become an important partner as regards foreign investment, although its investment contribution has so far been limited (around US\$0.44 billion in 2015). The still unresolved territorial dispute over the Kuril Islands had been a key barrier for years; however, Moscow managed to convince the Japanese to change their approach, separating the territorial disputes from economic co-operation⁶⁵. Tokyo is interested in developing energy co-operation, proof of which includes the preliminary agreements signed with Russia, for example, one concerning the construction of the third production branch as part of the Sakhalin-2 project, as well as agreements between Japanese firms and Rosneft on the development and operation of the fields located in the Sea of Japan⁶⁶. Furthermore, talks on building a gas pipeline running from Russia to

⁶⁴ Дальний Восток испытал прилив инвесторов, <http://www.kommersant.ru/doc/3080905>

⁶⁵ For more information on the evolution of political relations between Russia and Japan, see: W. Rodkiewicz, The turn to the East. The flawed diversification of Russian foreign policy, *OSW Point of View*, 6.10.2014, pages 25-27; <https://www.osw.waw.pl/en/publikacje/point-view/2014-10-06/turn-to-east-flawed-diversification-russian-foreign-policy>

⁶⁶ In May 2013, Rosneft and Japan's INPEX signed an agreement on establishing a joint venture tasked with operating oil fields on the Sea of Okhotsk; <https://rosneft.com/press/releases/item/185095/>

Japan have been underway for many years, which was confirmed on the occasion of President Putin's visit to Japan on 15–16 December 2016.

At the same time, many factors preventing the influx of foreign investments exist at present. The main barriers stem from the geographical characteristics of the region – small population density, still poorly developed infrastructure and harsh climatic conditions, which generate additional costs for potential investors. Another crucial element is the lower competitiveness of the Russian proposition which also concerns those sectors where trade relations were traditionally intense. For example, small and medium-sized entrepreneurs from Japan began withdrawing from buying timber and derived products from Russia and are instead choosing Canadian manufacturers who offer more competitive prices. Political impediments also have a great impact. Since the Russian aggression against Ukraine, investment opportunities have been restricted by the sanctions imposed on Russia by the USA, the EU and such countries as Canada and Japan. Furthermore, the unresolved Kuril Islands issue – despite the suggestions that the stance has been changed – remains a barrier to qualitatively significant investments in the case of Japan. This has been proven by the limited economic effects of the aforementioned visit to Tokyo by President Putin in December 2016⁶⁷. On top of that, the issue of using existing transit routes is also essential in the case of Japan; most of its exports are supplied to Russia via the Baltic Sea and not through the Far East. This is mainly a result of the fact that it is the European part of Russia that is the main outlet for Japanese goods (automotive products, machine-building and electronic industries).

Another limitation preventing the region's economic development is the small internal market which is insufficiently appealing to investors. The vast distances and high costs of transport to the distant central regions of Russia and the shortage of qualified workforce make many investments targeted at the internal market unprofitable. Both investment and individual consumers' demand is predominantly geared towards competitive products from imports, especially from China, Japan and South Korea (machines and equipment, cars, construction materials, clothes, food and miscellaneous).

⁶⁷ For more information see: W. Rodkiewicz, Russia-Japan: no breakthrough on the Kuril Islands, *OSW Analyses*, 21 December 2016, <https://www.osw.waw.pl/en/publikacje/analyses/2016-12-21/russia-japan-no-breakthrough-kuril-islands>

CONCLUSIONS

Since Vladimir Putin took power, the Far East region has gained political significance in the context of the priorities of Russia's domestic and foreign policies. At the same time, the lack of a clear comprehensive development concept means that a development model based on raw materials is being implemented in practice, which fits in with the reality of the state policy at the federal level. One of its consequences will certainly be an intensification of trade with foreign partners (China, Japan and India) interested in imports of Russian oil and gas. However, actual growth may be much lower than forecasted, especially considering the existing trends in the Chinese energy sector. The present trade dynamics suggests that cross-border contacts with frontier areas will most likely be strengthened at the expense of weakening economic ties with other regions of Russia.

On the other hand, it is hard to envisage that a model based upon raw materials would be capable of ensuring a high growth rate and macroeconomic stability over the longer term. It will certainly not contribute to the development of research and technology. Although numerous universities and academic institutes operate in the region, the results of their work have no major impact on improving the economic situation there. This is because the state-owned companies active in the region that focus on earning as much as possible from raw material production are not interested in the results of such institutions' work.

At present, there is no risk of the region's marginalisation as witnessed in the 1990s. At the same time, it is increasingly unrealistic that the uncompetitive Russian Far East might become an important and effective instrument for strengthening Russian economic influence in the Eastern Asia region. At present, there are no prerequisites that would allow one to assume that the economy of the Russian Far East could become competitive to the increasingly rapidly developing northern provinces of China or South Korea and Japan, either in the medium or long term. Therefore, it appears that political reintegration of the region with the centre of the federation, and the status of a stable raw material base for Asian countries, currently represents the maximum development potential of the Russian Far East.

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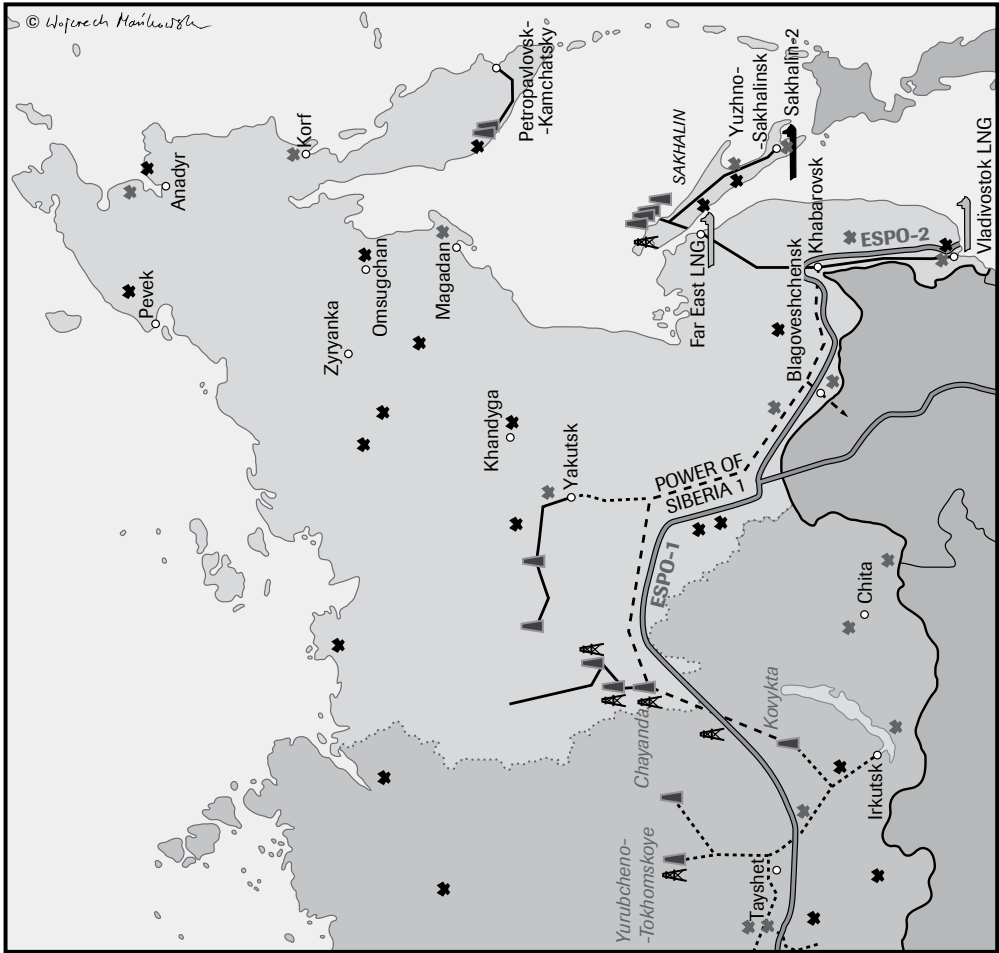
APPENDIX

Map 1. Economic potential of the Far Eastern Federal District



- metallurgical industry
 - ⚙️ coke and nuclear materials production
 - 🏭 chemical industry
 - 🏠 food industry
 - 🔧 machine and equipment production
 - 🌲 timber industry
 - 📄 paper industry
 - 🏢 research and development centres
 - ⚡ hi-tech industry
 - ⚙️ metal and mineral ore deposits
 - 🌿 production of bioresources
 - ⚓ river and sea ports
 - ★ transport and logistics hubs
- * Vladivostok and adjacent ports: Nakhodka, Vostochny and Kozmino
- ** Ports: Vanino and Sovetskaya Gavan

Map 2. Russian Far East – infrastructure and energy resources



- existing oil pipelines
- A oil fields
- ▲ gas fields
- existing gas pipelines
- - - gas pipelines under construction
- ⋯ planned gas pipelines
- ➔ LNG terminals
- ➔ LNG terminals under consideration
- * hard coal deposits
- ★ lignite deposits