As an APEC Summit Nears, So Does a Moment of Truth For Putin and Russia in Asia
By Nodari Simonia & Victor Sumsky

The September summit of the Asia Pacific Economic Co-operation forum in Vladivostok marks a potentially historic turning point in Russia’s relations with Asia. At a symbolic level, the massive infrastructure being built for the summit showcases a commitment, spearheaded by President Vladimir Putin, to pushing the country away from its Eurocentric past to a new reality that embraces Russia’s economic potential in its own Far East and in a rising Asia.

Nodari Simonia and Victor Sumsky delve into the complex politics and economics of Putin’s bold strategy to turn Russia toward the East.

IN APRIL 2012, VLADIVOSTOK — the capital of Russia’s Maritime Province and the country’s Pacific gateway — witnessed a landmark event. The construction of a cable-stayed bridge over the Eastern Bosphorus Straits that separates the mainland part of the city from Russky Island, until recently a military base, culminated in the installation of the last deck section. This operation effectively brought into being a masterpiece of infrastructure. The central span of the bridge extends to 1,104 meters. It is the longest element of this kind in the world, and some technologies that had to be applied to create it are unique. By July, the paving works should be finished, and the bridge will be opened for traffic — right in time for the APEC Summit scheduled on Russky Island for early September.

A brand new symbol of Vladivostok, this bridge is actually more than that: it’s a sign of Russia’s determination to finally make it in Asia by systematically modernizing Siberia and the Far East in close co-operation with the country’s Pacific neighbors. And it is not the only such sign. More than 50 other projects, with a total cost of 600 billion rubles (about $20 billion) must be completed before the summit in order to sustain Vladivostok’s transformation into a booming megacity. Among these projects are the spacious premises on Russky Island where the summit is to take place. Once the VIPs go home, this site will be turned into a campus of the newly created Far Eastern Federal University, conceived as a hub of excellence and innovation in the Asian part of Russia.

The domestic political background for all this is President Vladimir Putin’s victory in the March 4 presidential elections. In fact, a whole number of Putin’s recent initiatives and statements (of which we shall say more later) point to the fact that he is concentrating on two interrelated priorities: establishing a new base for Russia’s socio-economic development in Siberia and the Far East and opening this area up for interactions with dynamic Asian players.

If this assumption is valid, then why is this scenario becoming a realistic possibility only now, at the start of Putin’s third presidential term?

PUTIN: A PRACTICING EVOLUTIONIST
In a world where revolutions (or whatever is presented to the public under that name) are suddenly in vogue again, post-Soviet Russia must stick to its own, non-revolutionary agenda. In a sense, the whole period of Soviet history between 1917 and 1991 can be described as an emergency, initially created by World War I and the Bolshevik Revolution, and later sustained by World War II and its continuation in the form of the Cold War. Attempts to get over this emergency by putting the country on the track of evolutionary development were undertaken more than once. Some of them seemed to work for a while, but none of them ever worked fully. Whatever might be the reasons for that failure, its ultimate manifestation was the breakup of the Soviet Union. While Boris Yeltsin’s era might look to a superficial external observer as a belated step toward normalcy, for millions of Russians it was hardly that. The spirit of these times, marked by zealous anti-Sovietism, pro-Western daydreaming and neo-liberal orthodoxy at the top (not to speak of general economic decline and poor governance), was anything but evolutionary. Rather, it smacked of a clumsy counter-revolutionary rollback.

At the dawn of the 21st century, the nation was literally crying for order and justice at home and a dignified stand in the world. However, responding to that strong demand in a hasty, impulsive way could only be counterproductive. Paradoxically, any new Russian leader, who would not want to be a prisoner of his flamboyant predecessor’s heritage, could not afford an abrupt breakaway from the past. He had no choice but to move away from it in a cautious and calculated, step-by-step fashion, with a clear understanding of his own limitations and the country’s urgent needs, always seeking a healthy balance between elements of continuity and change. To make a long story short, this leader had to be a practicing evolutionist. Looking at the whole period of Putin’s leadership, now spanning more than a decade, one may safely say that this is the phrase that best describes him.

Putin’s major preoccupation in his first years in power was to bring the state back to its senses, to restore the country’s governability and the economy’s growth. This mammoth task did not seem to leave much time for anything else. Nevertheless, with every passing year it was becoming all the more clear that the president, being aware of his country’s complex Eurasian identity and opportunities for growth through partnerships not just with the West, but with neighbors in the East as well, was seeking to diversify Russia’s external links. Characteristically, working trips across the Urals, to Siberia and the Russian Far East, were becoming the norm of Putin’s presidency, just as were official visits to China, India and some other Asian countries rarely or never visited by top Russian statesmen in the past. Putin’s annual appearances at APEC summits since 1999 also contributed to a better understanding of Russia’s genuine interests in the Asia-Pacific.

In fact, the idea of hosting the APEC summit in Vladivostok belonged to Putin himself, showing how serious he was about looking eastward — both inside Russia and beyond its borders. For him, all sorts of local preparations for this event...
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were a chance to start creating a mechanism that would give a steady impetus to the rise of Russia’s Asian fortunes. That is why he would not listen to a chorus of “Russian Europeans” who tried to talk him out of investing hugely in Vladivostok’s development and pointed to St. Petersburg and Moscow with their metropolitan glamour as much better venues for the summit.

But the APEC summit could not be an end in itself. The event would have looked rather empty against the background of stagnating external trade and meager investment flows. A pragmatist of Putin’s caliber could not possibly miss this point. Something had to be done to energize economic relations with Asia well before the summit. Putin shrewdly responded (and continues to respond) to this challenge by playing the same trump card that he already played in Europe with obvious success. The name of the card is energy.

**ESPO? WHAT’S THAT?**

The abbreviation stands for Eastern Siberia–Pacific Ocean pipeline system designed and constructed to export crude oil from Russia to China, Japan, South Korea and other Asia-Pacific markets. By some accounts, in the decades to come this project will be as crucial for Russia’s Asian fortunes as the famous Trans-Siberian Railroad used to be a hundred years ago. Practical preparations for construction started in 2003 (that is, four years before the official decision to set the APEC summit of 2012 in Vladivostok). The first section of the pipeline, covering a distance of 2,700 kilometers between Taishet and Skovorodino, is already in operation, from Skovorodino to Kozmino crude oil terminal in railway tanks. Apart from a stable flow of oil from Russia to China, the opening of ESPO (along with some other energy projects in the Far East, notably those on the island of Sakhalin) is already resulting in other significant changes. Suffice it to say that due to growing imports of Russian oil, Japan has got a real chance to decrease its dependence on shipments from the Middle East. The Japanese have been trying to solve the problem of their dependence on the Middle East since the oil shock of the 1970s, but no matter how hard they tried, the share of Middle Eastern suppliers in Japan’s imported oil continued to rise, going beyond 87 percent. In 2006, when Japan began purchasing oil from Sakhalin, the share of these shipments in its oil imports was just 0.7 percent. One year later, it increased five-fold, reaching 3.5 percent. In 2010, with the start of ESPO shipments from Kozmino, Japanese imports of oil from Russia amounted to 14.5 million tons, or 6.4 percent of its total oil imports. Simultaneously, for the first time ever, the share accounted for by the Middle East declined to below 80 percent.

Statistics related to the dynamics of foreign sales of liquefied natural gas (LNG, in million tons per year) produced by Sakhalin Energy, the operator of Sakhalin-2 project, tell a similar story (see Table 1).

<table>
<thead>
<tr>
<th>Exported to</th>
<th>Million tons per year</th>
<th>2009</th>
<th>2010</th>
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<tbody>
<tr>
<td>Japan</td>
<td>3.69</td>
<td>8.23</td>
<td></td>
</tr>
<tr>
<td>China</td>
<td>0.25</td>
<td>0.51</td>
<td></td>
</tr>
<tr>
<td>South Korea</td>
<td>1.35</td>
<td>3.90</td>
<td></td>
</tr>
<tr>
<td>Taiwan</td>
<td>0.24</td>
<td>0.67</td>
<td></td>
</tr>
<tr>
<td>India</td>
<td>0.67</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kuwait</td>
<td>0.41</td>
<td>0.09</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>6.61</td>
<td>13.40</td>
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Compared to Middle Eastern and African shipments of hydrocarbons, growing Russian supplies of oil and natural gas to Asia-Pacific markets have some unquestionable advantages. First, there is no threat of a seizure by pirates near the shores of Somalia and the Gulf of Aden, no loss of time and money following such incidents, no need to pay for naval patrols in that area. Second, in every conceivable case, the distance separating the supplier from the client will be much smaller. Thus, both the time of delivery and transportation expenditures will be smaller. Third, as a supplier, today’s Russia is much more reliable than competitors in those parts of the world where conflicts and instability spread across borders like viruses.

**TRANS-KOREAN PROJECTS**

Talking about Russia’s efforts to redirect some of its energy exports to the East, it is impossible not to mention the Trans-Korean gas pipeline, 1,100 km long and planned as an extension of the Sakhalin-1–Khabarovsk–Vladivostok pipeline. This project is usually discussed in a package with the Trans-Korean railroad (planned as an extension of the Trans-Siberian Railroad). Since both the pipeline and the railroad are supposed to go from Russia to South Korea through North Korean territory, the importance of these schemes cannot be measured just by stable supplies of gas or livelier transit of goods. Implementation of the Trans-Korean projects might contribute to a new atmosphere of co-operation on the Korean Peninsula, and eventually help to do away with a major geopolitical impediment to economic integration in East Asia.

Table projects had been offered more than once to both the North and the South, and more than once both the North and the South expressed their approval. South Korea demonstrated its no-nonsense attitude towards this offer by building its own section of the railroad which now ends near the border with the North, and last October Russian Railroads ran a trial train along the upgraded trans-border route between Russia’s Khasan and North Korean Rajin.

Until lately, America’s negative attitude would not permit the Trans-Korean projects to go beyond the stage of talks. Every time there were signs that the North and the South were coming to terms, the US would invariably do something to provoke a break in their contacts. All this created a pessimistic aura around the projects and a widespread perception that they were doomed. However, some recent developments seem to give reasons for cautious optimism. In August 2011, then Russian President Dmitry Medvedev met with North Korean leader Kim Jong-il in Ulan-Ude, not far from Lake Baikal, to discuss the problems of Asian security and the prospects for a dialogue between the two Koreas, as well as Russian assistance to North Korea. Once again, Trans-Korean projects were a major agenda item — just as in early November when Medvedev had a meeting with his South Korean counterpart, President Lee Myung-bak, in St. Petersburg. Soon after that, Victor Ishaev, the Russian President’s Representative in the Far Eastern Federal Region, disclosed that Kim Jong-il was supporting the construction of the Trans-Korean pipeline and that North Korea might be getting $100 million annually for the transit of gas.

In a parallel development, from July 2011 Pyongyang and Washington began to talk to each other in earnest. For a while, it looked as though...
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US Secretary of State Hillary Clinton was determined to correct the mistake of her spouse, ex-US President Bill Clinton, who once postponed an already prepared trip to North Korea hoping to get there later but never making it. But then, the death of Kim Jong-il and the proudly announced but unlucky launch of a North Korean space satellite resulted in new uncertainties about the fate of Trans-Korean projects. Who knows what may happen next, but Russia’s stake in both these projects is too high to give up — especially now, when not just top officials but Russian business and academia are focused on Asia like never before.

LOOKING EAST — AND BEYOND RAW MATERIALS

A combination of several overlapping factors and trends is making Asia a popular subject in domestic debates about Russia’s options in the world of the early 2010s. The global financial and economic crisis that has hit the US and the European Union so badly, plus a critical mass of accumulated disagreements with them, pushes the Russian elite (or at least some sections of it) to conclude that for the time being Russia has reached the limit of what is possible in its co-operation with the West. Growing numbers of thinking Russians are finally coming to realize what the rest of the world discovered much earlier: the global economy’s center of gravity is indeed shifting towards East Asia. The more familiar they become with this region the more they feel that it is relatively free from Russia-related phobias and fears so typical of Europe. Some influential intellectuals as Sergey Karaganov and Vyacheslav Nikonov, who had not been known until recently for expertise in Asian affairs, are now publicly advocating adjustments in Russia’s internal and foreign policies that will favor co-operation with a rising Asia. The urgency of these adjustments is all the more clear due to a disturbing asymmetry between the poorly developed Far Eastern territories of Russia and the vibrancy of modernizing China. Remarkably, those very critics who are alarmed by this problem tend to agree that it cannot be solved in the absence of stronger linkages with Asia, diversified beyond the sale of hydrocarbons and other raw materials.

Short- and mid-term government plans for Siberia and the Far East now include development of modern petrochemical production; the upgrading of existing transportation routes, sea and airports, along with creation of totally new infrastructure and communication systems; promotion of export-oriented agriculture to respond to the growing demand for food in Asian markets; development of industries to supply equipment and machinery for all of the above; creation of clusters of hi-tech production and services (such as Vostochny space launching site in Amur Region).

Could the government carry all this out alone? Obviously not, even if it were more efficient than the government of Russia as we know it today. In fact, the more efficient it is, the bigger would be its ability to launch a public private partnership (PPP) for such purposes as those outlined above. Does Russia, with all the multi-billion-dollar reserves it has accumulated due to massive exports of oil and gas, have enough money to finance modernization of its Asian regions? Once again, the answer is no, but foreign investments can definitely be mobilized when the international investment climate improves. A well-functioning PPP would be the best of all possible proofs that it does.

Last but not least, who will be responsible for co-ordinating PPPs, attracting foreign capital and, of course, drawing up the integrated strategy of Siberian and Far Eastern development? Let’s not forget that we are talking here about transforming the socioeconomic realities of enormous territories. This may not be possible without a very special vehicle combining a strong sense of purpose and co-ordination with operational flexibility and freedom from bureaucratic routine.

With this in mind, let us see what Putin has been trying to do to create such a vehicle.

THE EASTERN CORPORATION

In 2010, Putin, at that time still prime minister of Russia, initiated the formation of an entity called the Far East and Baikal Region Development Fund, with an investment capacity of 70 billion rubles ($2 billion) in the period up to 2015 coming from the state. Implementation of this project, officially based on the PPP principle, was entrusted to Vladimir Dmitriev, Chairman of the Board of state-owned Vnesheconombank (VEB). After a year or so, nothing much came out of it — primarily because the private sector did not like the idea of investing its money under bureaucratic guidance. Past experience had shown that in the framework of such “joint ventures,” the representatives of ministries and state-owned banks had been only too willing to “dissolve” the money from private sources in all sorts of blurred “territorial development” schemes instead of pointedly investing them in particular projects. This kind of practice was widely seen as wasteful and abusive. When First Deputy Prime Minister Igor Shuvalov called potential private investors to the government headquarters to discuss the situation, all of them openly refused to contribute to the Fund. At the same time, they expressed their readiness to interact with the state as equal partners in projects that would represent mutual interest. Thus, the VEB-administered Fund was not getting anything but the money provided by the state.²

Reacting to this turn of events in November 2011, Putin instructed then Minister for Emergence Situations (and now Moscow Region Governor) Sergey Shoigu to prepare a blueprint for an “Autonomous State Corporation” to develop Eastern Siberia and the Far East. With the geographic area of responsibility spanning from the Western border of Krasnoyarsk Province to the Pacific coast, this corporation was to function under the aegis of a Supervisory Board nominated by the Russian president and personally chaired by him.

² Dal’nevostochniy Kapital, Vladivostok, № 1, 2012.
In January 2012, Shoigu submitted his draft to Putin. After the government generally approved the document, it was up to the Ministry of Economic Development to polish it. This they did in about two months. But even before that job was completed, some of the spokesmen of the Russian “liberal elite” began to express their disagreement — if not outright opposition — with the plans of Putin, who by now was not just the prime minister, but the president-elect as well. At the forefront of this campaign was ex-Finance Minister Alexey Kudrin. His invectives against Putin’s new project were widely spread by Vedomosti — the Russian-language daily jointly published in Moscow by The Wall Street Journal and the Financial Times and strictly following their party line. Kudrin insisted, for instance, that the proposed state corporation could only inhibit the development of the region because other players willing to work there would face an unbeatable competitor. Another bizarre statement was made by Vladimir Mau, a close associate of late Yegor Gaidar, who had been Yeltsin’s economic guru in the early 1990s. According to Mau, the future of Siberia “must be determined by the people of Siberia themselves, and it is up to them to make their life orderly. And basically it is an issue that has to be addressed by local administrations.” Mau, who is the rector of the prestigious All-Russian Academy of National Economy, was practically saying that development of more than two-thirds of Russia’s territory should be carried out by fewer than 30 million local inhabitants and that the federal government was not a fully legitimate participant in this project.

The real information bomb exploded on April 28. On that day, Finmarket news agency reported that the blueprint for the new state corporation had “outraged” some high-ranking officials who did not bother to hide their feelings, even though they were fully aware of the project’s origins. According to the report, the Minister of Finance Anton Siluanov was as rigidly opposed to Putin’s initiative as his predecessor Kudrin, and had expressed his views in a special letter, addressed to First Vice-Premier Shuvalov. The Minister’s argumentation was based on the claim that the proposed corporation with its “vague objectives and functions” would usurp the prerogatives of federal ministries, resist financial control and severely disrupt the established process of governance. In case a special body to deal with the development of Siberia and the Far East was considered essential, concluded Siluanov, a federal agency to co-ordinate the activities of other governmental units in that realm should be enough.

If Finmarket’s story is to be believed, the addressee was receptive to the message: he publicly said that, at the end of the day, a special corporation might not be needed, and its tasks might be given to the Far East and Baikal Region Development Fund.

WHY THE BUREAUCRATIC PROTEST?
So what was going on? Why did the influential opponents of Putin’s initiative, both inside and outside government, behave as boldly as they did?

First, the estimated funds of which the future corporation would be in charge were really huge. Initially these might amount to 1.3 trillion rubles, primarily intended for infrastructure projects. And that was not all, since project financing was also expected to come from private sources, both domestic and foreign. Behind the bureaucracy’s opposition to the creation of the corporation were palpable fears that it would lack control over these financial flows.

Second, among the major stumbling blocks on Russia’s road to modernization is the proverbial “inter-ministerial co-ordination.” The suffocating effect of this procedure, cultivated through the years by the “liberals” of Kudrin’s school, should be known to Putin all too well. What else if not this inner knowledge was prompting him to assure that his Eastern Corporation would not be subject to formal control and would not be crushed by it, unlike some other potentially useful initiatives? If, due to Putin’s determination, the corporation could start to function as planned, the consequences of its activity — such as accelerated transformation of Russia’s Asian territories and the system of its external partnerships — might someday make the system of bureaucratic capitalism inherited from Yeltsin unsustainable. Were the proponents of the status quo capable of looking that far? Maybe not, but their instincts for self-preservation were certainly sharp enough to tell them that the system was being challenged, and they could not help but react.

Last but not least, the pro-Asian momentum of Putin’s plan quite clearly irritated the “liberals” with their well known pro-Western sympathies.

TO BE CONTINUED ...
How staunchly were Putin’s critics prepared to resist his plan? How tolerant or how firm would he be in this situation? Would or would not there be the Eastern Corporation? These and similar issues were preoccupying the pundits before and after Putin’s May 7 inauguration, prior to the formation of the new Russian government.

When the composition of the new cabinet was finally announced on May 21, it became clear that a kind of compromise had been achieved. While both Shuvalov and Siluanov retained their previous positions, a totally new governmental entity was formed, the Federal Ministry for the Development of the Far East, with Victor Ishaev as its head. The ministry will be responsible for the progress of the nine subjects of the Russian Federation covering up to 36.3 per cent of the national territory — an area almost half of what the Eastern Corporation was supposed to develop.

Nevertheless, the official status of this new structure is obviously higher than the status of a federal agency (to which Siluanov was prepared to agree, at best), not to speak of the fact that Min- ister Ishaev, a long-time governor of Khabarovsk Province, is a highly experienced manager and a figure of national stature. The regulations for the new ministry are yet to be officially approved, but according to press analysis of the draft submitted by Ishaev to the government, the sum of its prerogatives might make the new body comparable in power to the strongest federal ministries (including the Ministry of Finance).7

As for the Eastern Corporation, since mid-May, the government’s spokesmen have been pointedly avoiding comments about the possibility of its launch. Up to now, it is an open-ended question. No doubt, the struggle over the development of Siberia and the Far East, as well as Russia’s future in Asia, is a story to be continued. But judging by what we already know of Putin — and noting how these themes perennially reappear in his post-election statements — one may hope that he will act as befits a leader who faces a moment of truth.

3 See Shoigu’s extensive interview in Kommersant, Moscow, April 23, 2012.
4 Vedomosti, Moscow, April 25, 2012.
5 Nezavisimaya Gazeta, Moscow, February 20, 2012.
7 Kommersant, June 4, 2012.