

South - Eastern Shift

in complement of our previous reports

China and Russia share some 4,000 kilometers of common border, and their neighborly relationship has certainly had some ups and downs. But it's clear to me that the opportunities for cooperation between these two nations have enormous potential mutual benefits, particularly in the trade of natural resources.

We first saw significant signs of Russian interest in Asia's capital markets when the oligarch Oleg Deripaska floated his aluminum company onto the Hong Kong Stock Exchange in early 2010. In 2011, he obtained a US\$5 billion memorandum of understanding with China's Export Import Bank for resource developments in Siberia and Russia's Far East region, including power generation plants, coal mines and other projects.

Recognizing the economic problems in Europe and Asia's stronger relative growth rates over the past few years, Russia's leaders have directed their focus eastward and to their vast territory stretching all the way to the Pacific Ocean. See our comment [RUSSIA CALLING! Part 2](#)

In April 2012, the Russian government also passed legislation to form a US\$17 billion Far East corporation, partly exempt from federal jurisdiction and reporting directly to the president. This new entity was given special powers to form new businesses and allocate resources to develop the area.



In addition, an US\$8 billion space center is planned for the Amur Region just 60 miles from the Chinese border. This will replace the launch site in Kazakhstan which is now used primarily by the Russians and Americans to travel to the International Space Station. The Amur project will include seven launch pads with the first rocket launch planned for 2015.

Railroads and Oil Fields

These are just a few examples; the Russians have planned a number of other sizable Far East and China-related projects. I think the extension of Russian railroad lines to China could turn out to have the most significant long-term beneficial impact resulting from cooperation between the countries. The Russians have signed joint venture agreements with Chinese railroad organizations to modernize the Russian rail corridor that links Europe with China.



I believe Russia's rich oil and gas fields would be of great interest to the Chinese, as energy demand there is expected to continue to rise with a growing middle class. With five trillion cubic meters in proven natural gas reserves in Russia's Far East, the possibilities for China are enormous. However, negotiations on the pricing of the gas are still ongoing. China has gas deals all over the world but the possibility of piping gas from Russia seems logically to make the most sense—if the price is right.

In Siberia, the Bazhenov structure has enormous reserves of oil—larger than even the huge Bakken oil-bearing rock in North Dakota and Montana in the U.S. The Bazhenov reserves cover 2.3 million square kilometers (the size of the U.S. state of Texas and the Gulf of Mexico combined) and it is 80 times larger than the Bakken (1), which is currently yielding more than 500,000 barrels per day (bpd). Russia's national subsoil agency, Rosnedra, has estimated that the Bazhenov shale formation could yield 182 billion barrels in total—and that's the low end of its estimates.



The Russian Energy Ministry estimated that by 2020, the Bazhenov could be producing up to 2 million barrels per day with the help of fracking technology, where the oil-bearing rock is broken under high pressure water and chemicals to release the oil. Russia and Saudi Arabia have shifted between first and second place globally in terms of oil production over the past couple years, with Russia producing 10 million bpd in 2010, compared with Saudi Arabia's 9 million.⁶ Development of the Bazhenov fields could raise the total substantially, with China likely being the prime market.

Conflict—and Cooperation

In another effort to emphasize Asian involvement, Russia succeeded the U.S. in the role of President of the Asia Pacific Economic Cooperation (APEC), the organization of 21 Pacific Rim nations. The 24th APEC Summit was held this year in Vladivostok near Russia's borders with China and North Korea, the home port of the Russian Pacific Fleet as well as Russia's largest port on the Pacific Ocean.

The city received an enormous boost with some US\$1 billion invested in a five-year infrastructure program including hotels, roads and other projects to improve the city and impress the APEC delegates. At the summit, a number of cooperatives were also announced. For example, President Putin praised the Russian-Japanese project to build a liquefied natural gas (LNG) plant in Vladivostok for exports of natural gas to Japan. (In 2011, Japan consumed 83 million tons of LNG.) The US\$7 billion Vladivostok plan will have a capacity of 10 million tons a year. Russia's other LNG plan is on Sakhalin Island, producing 10.6 million tons per year.



From a geographic perspective, Russia and China's common border along the Amur River is an area of past conflict but also one of potential cooperation. Russia's side is underpopulated but boasts arable land, timber and other resources while the Chinese side is densely populated with limited resources. In 1969, cross-border tensions nearly resulted in a full-scale war, but today the mood is quite different. Reports indicate that most Siberian and Far East officials are positive about the presence of Chinese in their regions since they are suffering from the departure of ethnic Russians from their areas, and the Chinese labor force can help cultivate the land.

Of course, even the friendliest of neighbors can disagree at times, but if neighbors like China and Russia can focus on projects to their mutual economic benefit, I think that's an approach we might pursue in our own backyards.

1. Source: Forbes, "Meet the Oil Shale Eighty Times Bigger Than the Bakken," June 2012.