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The views expressed in this study are those of the author and do not necessarily reflect the official policy or position of any official, unless and when the otherwise is specified as to be so. Comments pertaining to this work are invited and should be forwarded to elena_shadrina@yahoo.com.

Abstract

The article addresses Russia's state capitalism as pertaining to two aspects: spatial dimension and resource endowment. These two features are believed to substantially influence the formation of Russian government's contemporary policy. It is argued that external environment, in particular geopolitical situation in Northeast Asia, makes Russia's region-specific and sector-specific state capitalism not only possible, but potent of achieving the government's newly reasserted goals for the development of the Russian Far East, though with suboptimal outcomes. The article touches upon the areas where the theory of state capitalism has been advanced, explores Russia's state capitalism in the regional context of the Russian Far East, analyses the preconditions for Russia's reinvigorated optimism for energy cooperation with Northeast Asian states and discusses the outcomes of Russia's mode of state capitalism from energy cooperation with Northeast Asia.

*Key words***:** state capitalism, energy policy, Russia, Russian Far East, Northeast Asia.

Contents

Graphs, table and map

Acronyms

CNOOC – China National Offshore Oil Corporation
CNPC – China National Petroleum Corporation
ESPO - Eastern Siberia - Pacific Ocean (oil pipeline)
FEC – fuel energy complex
IEA – International Energy Agency
IEEJ – Institute of Energy Economics, Japan
IOC – international oil company
JOGMEC - Japan Oil, Gas and Metals National Corporation
MED – Ministry of Economic Development of the Russian Federation
MET – mineral extraction tax
MoF – Ministry of Finance of the Russian Federation
MoFA – Ministry of Foreign Affairs of the Russian Federation
MoE – Ministry of Energy of the Russian Federation
MoU – memorandum of understanding
NDRC – National Development and Reform Commission, China
NEA - Northeast Asia
NEA-3 – Japan, China, Korea
NOC – national oil company
PSA – production sharing agreement
SCO – Shanghai Cooperation Organisation
SINOPEC – China Petroleum and Chemical Corporation
SOE – state-owned enterprise

Units

mn - million
bn – billion
tn – trillion
b - barrel
bcm – billion cubic meters
t – tonne
$/t/km - $/ tonne/ kilometre

1. Introduction

A recognised expert on state capitalism Ian Bremmer (2009, 3) defines it as "*… an economic system in which governments manipulate market outcomes for political purposes. Governments embrace state capitalism because it serves political as well as economic purposes—not because it's the most efficient means of generating prosperity. It puts vast financial resources within the control of state officials, allowing them access to cash that helps safeguard their domestic political capital and, in many cases, increases their leverage on the international stage*."

Whether state capitalism is a new phenomenon? History tells us, not at all. Economic nationalism, whose features are quite reminiscent of what contemporary known as state capitalism, has been around the 17th century (Mishra 2012a, 2012b; Kurlantzick 2012). Dutch colonisers of Asia pioneered the way, and British merchants have advanced it even further during the Opium Wars. Germany practiced what could be described as state capitalism since the end of the 19th century. In the late 19th century, the United States, too, have attempted nurturing local industries under highly protective regimes and again actively employed state interventions during the 1930s' New Deal. The post-war European economies involved in the Marshall Plan familiarised themselves well with the workings of state capitalism. After the Second World War, newly liberated former colonies across the globe have been putting in place state capitalism's principal toolkit. In the late 1970s capitalist economies – France, the Great Britain, Japan, to a lesser extent the USA - were all known for the state's active involvement in markets. Since the 1980s, the waves of arrivals of different groups of emerging economies to the global marketplace have been revealing the achievements state capitalism is capable of. The aftermaths of the recent global crisis seem to have legitimised state capitalism renaissance as many market economies saw their governments resorted to stronger roles.

Traditionally, state capitalism has been juxtaposed with liberal market (in terminology of Aligica and Tarko 2012, democratic capitalism). As the years after the Lehman shock revealed state capitalism's quite contrasting with free market economies' performance, scholarly interest has reasonably addressed the nature and mechanics of contemporary state capitalism anew. While academic research tends to approach the theme from normative perspective critiquing the practices which state capitalism employs for intervening in economy, recent applied inquires meant to satisfy business community's practical concerns about sharpening competitiveness of businesses in state capitalism economies, on the other hand, involve the elements of microeconomic

analysis (The Economist 2012, Mishra 2012a, 2012b). Business-oriented analysis unveils that state capitalism in Brazil, China and India has started seriously challenging the market democracies increasingly competing with them in innovation-intensive sectors. The peculiarity of the moment is that while normative analysis pursues the idea that state capitalism is impinging upon free market economies, since its domestically spawn inefficiencies are unavoidably being transferred to the global marketplace (Bremmer 2009, 2010; Aligica and Tarko 2012; Musacchio and Lazzarini 2012), pragmatically-minded businesses invite the U.S. and European governments to learn from state capitalism systems (Kurlantzick 2012).

Russia is one of the economies which is exemplified as a typical case of state capitalism. This article employs the concept of state capitalism and, drawing on Russia's two most prominent denominators - spatial dimension and resource endowment, sets analytical frame on Russian energy policy. By doing so, the article presents a region-specific (the Russian Far East) policy mode within a sector-specific (energy) policy. It is demonstrated that although the Russian government realises the necessity for energy governance reform, in order to sustain, the heavily reliant on energy revenues state capitalism practices only a narrowly-defined mode of energy governance transition (temporal adjustments implemented upon a region-specific approach). The government's energy policy in the Far East can be interpreted as this very kind of effort to mitigate complex built-in inefficiencies. On the one hand, the Russian government seeks to economically revive the Far East and more actively utilise its potential for the domestic economy. In doing so, however, and this seems to be the only plausible option, the government needs to incorporate the external dimension into its Far Eastern policy. The idea of Russia's (Russian Far East) integration in Northeast Asia (NEA) is certainly not a new vision; various scenarios have been contemplated in the last decades. The reality, nevertheless, is that NEA may well stand out as one of the least integrated regions. At this front, too the article argues, contemporary energy geopolitics of NEA indirectly favours Russia's energy state capitalism, permitting the transmission of Russia's sector-specific (energy) and region-specific (the Russian Far East) inefficiencies to the NEA economies.

In the subsequent sections, the article examines region-specific/ sector-specific[2] mode of Russian state capitalism. The article first briefs on theory of state capitalism. It further addresses the Russian case in energy sector, illustrating that energy policy is

[2] "Region-specific" context implies the Russian Far East and "sector-specific" scope denotes energy sector, not in its entirety but such as including oil and gas.

not homogeneous and varies across the regions. The external dimension of Russian energy policy is analysed in the context of NEA. The concluding part presents some policy implications and recommendations.

2. Theory of state capitalism

2.1. System, concept and category

Studies on theory of state capitalism can be broadly divided into two groups, namely those implemented during the era of capitalism vs. socialism rivalry (Dupuy and Truchil 1979) and those conducted after the demise of socialist system (Bremmer 2009, 2010; Aligica and Tarko 2012; Musacchio and Lazzarini 2012). Early work were primarily concerned to clarify whether state capitalism is a new type of economic system or it is a new category that can be treated within the existing theoretical frameworks. Naturally, free from ideological component more recent studies have been centred on the analysis of economic viability of state capitalism. Contemporary research is not as homogeneous, but made of two streams of which one is more focused on theory and another contributes to the body of applied studies (The Economist 2012). The latter has grown significantly after the Lehman shock, when struggling to cope with the crisis economically advanced countries have realised that state capitalist economies were not impacted as negatively or were able to recover relatively quickly.

Defining state capitalism it is worth noting that majority of early, as well as recent theoretical studies converge on the point that state capitalism does not reveal features which allow to qualify it as a separate type of economic systems (Dupuy and Truchil 1979, Aligica and Tarko 2012). Nonetheless, Bremmer (2009, 2010), who develops structural and operational dimensions of state capitalism, refers to it as an economic system in its own right.

Attempting to determine whether or not theoretical platform of state capitalism explains social structures of three qualitatively different types of countries[3] – advanced capitalist, Third World and socialist, Dupuy and Truchil addressed the diversity of appearances of state capitalism as far back as in 1979. Dupuy and Truchil's (1979, 2) main conclusion was that a new concept is not warranted, because "*…the various phenomena can be explained in terms of the logic of capitalism and socialism*". Conducted over three decades ago the study, nonetheless, advances some ideas which seem to be of relevance to the topic at hand. To start with, state capitalism is not as homogeneous. Rather, state capitalism has always had its peculiarities across (and even within) the three types of economic systems.

State capitalism in Third World (Algeria, Brazil, Colombia, Ethiopia, Libya, Mexico, Peru,

[3] Different in terms of dominant social relations of production.

Venezuela) arose on the waves of increasing anti-imperialist struggle and a search for a non-socialist alternative to dependency. Because the industrialisation required massive financial injections, greater state intervention achieved through the nationalisation of the natural resources has become one of the central elements of state economic policy. Military and the bureaucracy have played a significant role in the administrative apparatus of the state. Nonetheless, state intervention did not displace the dominance of private (national and foreign) capital, which mainly concentrated in agricultural and commercial sectors. Private business generally supported regimes with their centralised state apparatus, because this way private economic activity was more likely to be protected against certain types of risks. For these reasons, capitalist nature of economic systems in Third World (with several exceptions) has not been altered (Ibid: 4). At the same time, dependence on foreign capital, and even much more on foreign technology, know-how, machinery, etc. continued and deepened. For the sake of industrial development, state capitalism in Third World was forced to collaborate with the foreign capital in the form of joint ventures with the state controlling the majority of shares (51 percent), the package deals, and the likes. Eventually, state capitalism in Third World spawned a new type of dependency – on foreign finance and technology - and inflicted serious constraints on state planning and regulation of the economy.

To better identify the nature of state capitalism in the so-called advanced nation-states, Dupuy and Truchil emphasise the role monopolies play and, therefore, speak of state-monopoly capitalism. The fundamental features of state monopoly capitalism are the state's regulation of credit and money, taxation, subsidies, loan guarantees, government sponsorship of academic research which eventually is utilised by private capital, military and financial protection of foreign investments, etc. (Ibid: 15). At the early stages of capitalism, i.e. competitive capitalism, the state provided general prerequisites for capitalist development (transportation and communication, monetary, education, etc. systems). Over time, however, depending on economic development agenda, the state tends to favour the interests of certain sectors at the expense of others. Also, the state intervenes to help capitalist reproduction in the areas of armament production, environment protection, infrastructural projects, planning and anti-cyclical programs, foreign aid and guarantees of foreign capital investment, etc. The state assumed most of the costs and risks, thereby contributing to the efficiency of capitalist production.

As regards the relations of production in the socialist economies, Dupuy and Truchil argue that state capitalist can be applied only as an analytical category (Ibid: 32). They

specifically point that, different from two other types of economic systems, capitalist production relations and forms of distribution exist only in certain sectors of socialist economies, such as consumer goods production and agriculture, but they do not predominate to characterise sector of capital goods; the central planning erodes those sectors' commodity character; and state bureaucracy cannot be perceived as a capitalist class as it neither accumulates means of production nor purchases the labour force for its own ends. At the time of writing in the late 1970s, the authors expressed interest to see the analysis of the processes and conditions by which state bureaucrats could transform themselves into state capitalists. Later on, the task has been attempted by many (Luttwak 1990, 1999; Bremmer 2009, 2010; The Economist 2012; Aligica and Tarko 2012; Musacchio and Lazzarini 2012).

In a post-Lehman stream of work on state capitalism (which apparently was strongly prompted by a practical interest), studies by Aligica and Tarko (2012) and Musacchio and Lazzarini (2012) occupy a special place. Scrutinising contemporary state capitalism upon a comparative prism, these two works advance theoretical perspective of the subject. Aligica and Tarko's argue that contemporary state capitalism simultaneously reveals features of different economic systems and, more specifically, exhibits a great similitude with real life socialism. The authors' attempt to relate state capitalism and mercantilism results in a proposition that state capitalism is a version of (neo)mercantilism, and is a case of a rent-seeking system. Aligica and Tarko support Dupuy and Truchil's main conclusion: it is not warranted to treat state capitalism as a new economic system. Musacchio and Lazzarini reasonably observe that Bremmer's vision of state capitalism is somewhat incomplete, because in his analysis state capitalism is juxtaposed with perfectly competitive market, which is not the case even in the most advanced market economies.

2.2. Origins and growth

The origins of state capitalism can be different. References to economic history suggest that most of the time emergence of state capitalism signifies the government's resolve to handle rather harsh economic situation, which can be inherited by a young sovereign state as a part of its colonial history, resultant from the wars and military conflicts, aggravated by domestic or international crises, or be an interim condition during the transition period. Indeed, the prerequisites can be various, but the features of state capitalism are common: more centralised economic policy making and more actively practiced measures of direct intervention in economy.

Contemporary state capitalism relies on such primary actors as: national oil corporations (NOCs), state owned enterprises (SOEs), privately owned national champions, and sovereign wealth funds (SWFs) (Bremmer 2009, 2010). In sectors such as oil and gas, for instance, SOEs play by far significant role. That is to say, the 13 largest state-owned oil companies hold the grip on over the three fourths of the world's oil reserves and production. Privately owned multinational companies now produce about ten percent of the world's oil and hold some three percent of the global reserves (The Economist 2012). Contrary to popular belief, state capitalism does not necessarily have full control over certain assets. Musacchio and Lazzarini (2012: 12) distinguish between two modes: Leviathan (the state) as a majority investor (mostly, the case of SOEs) and Leviathan as a minority investor (SWFs, pension funds, life insurance funds, loans provided by state-owned banks, minority stakes in state-owned holding companies, minority stakes in partially-privatised firms – national champions, etc.).

On the typology of state capitalism, Bremmer (2010) propagates four-wave evolutionary development vision of state capitalism: geopolitically nurtured wave during the 1973 oil crisis, ideologically influenced wave during the 1980s when the socialist system has began collapsing, the mid-2000s wave during which many emerging market economies realised their strengthened financial power and started turning more assertive in political arena, and, finally, a fourth wave of state capitalism has been shaped by the global economic crisis.

Leaving apart historical context, Musacchio and Lazzarini (2012) focus on conceptual and logical content of state capitalism. Their four-mode notion of state capitalism is the result of probe into why does state capitalism exist. The authors distinguish between industrial policy, social, political and path dependence views. Economic perspective involves the development agenda, which is closely linked to implementation of industrial policy. Here, the government seeks to solve two types of market failures. The first is a lack of investment due to immature domestic financial market. Another problem lies with poor quality of coordination of productive investment. Socially concerned government intervenes while seeking the ways to handle short-term aspirations of profit maximisation minded private businesses. Pursuing political interests (stability, re-election, etc.) government can also be enticed to set about state capitalism toolkit. Finally, state capitalism, according to Musacchio and Lazzarini, can be influenced by rules, ties and ideologies that existed earlier. These four significantly differ from one another by their objectives, policy tools and performance. The latter is

examined rather thoroughly in four particular dimensions, namely, existence of agency problems, state capacity of coordination and enforcement of societal objectives in the economy, level of cronyism and the rigidity of allocations in the economy. A valuable contribution of Musacchio and Lazzarini's research is the analysis of the factors propelling one or another form of state capitalism. Examination of the factors defining the SOEs' performance within and across the sectors is attempted. Characterised as the least advanced in the contemporary research, this direction is described as one of the most timely for inquires topics.

State capitalism, as observed by Bremmer (2010), is bureaucratically engineered system which is particular to each government that practices it. The goals can indeed be various, but to attain them the governments invariably need the financial means. This logic is especially transparent in economies with rich natural resource endowment. There are, for instance, strong empirical evidences suggesting that government control over the petroleum sector is correlated with an economy's dependence on petroleum revenues (Tordo et al. 2011). It is however also established that countries that have large oil and gas resources face a more difficult task in the area of macroeconomic governance. The risk of Dutch disease becomes especially high when the inflow of foreign currency is substantial, because the population is reluctant to face austerity of the government's fiscal policy, instead expecting the state to become more socially responsible through the utilisation of accumulated natural resource revenues. Deepening dependence on resource revenues locks the government into even tighter control over the exploitation of the resource and political involvement in the NOCs' decision-making processes. Economic governance in the countries with high resource dependency seeks to use the SOEs/NOCs to finance budget gaps imposing for that end tougher financial burdens on them. In turn, forced to fulfil the state's financial claims NOCs, for instance, opt for dismissal of vital maintenance and exploration investment. Such a policy has critical implications for the long term sustainability of the NOCs, energy sector and the entire economy.

2.3. Modes of interaction

Since the late 1980s, many formerly closed economies have started opening doors to trade and investment. Not only the developed countries welcomed the trend but have started seeing it as an irreversible path. As Yergin and Stanislaw optimistically notice: "*The decamping of the state from the commanding heights marks a great divide between the twentieth and twenty-first centuries*" (2002: xiv). Apparently, too early has

state capitalism been addressed with the words of valediction. In the post-2008 world, the attainments of the proponents of state capitalism across the globe became so manifest that The Economist (January 21, 2012) devoted to the phenomenon a special report The Visible Hand.

On the account of modes of interaction between state capitalism and free economy, the debates unfold in two principal directions, such as the threat of state capitalism's political and/or economic dominance over market economies; and implications of state capitalism economies' internal inefficiencies on globalised free market economies.

At the times when ideology played a decisive (and dividing) role, there was no profound interconnectedness between different economic systems. Consequently, the free-market economies did not need to worry about competition from their non-market antipodes. Nowadays, much more globalised markets are no longer immune to external inefficiencies, such, for instance, as those born by economic policy-making in emerging-market economies. Bremer (2011, 2) argues that "*security is no longer the primary driver of geopolitical developments; economics is*". Contemporary environment has changed so that competition is unfolding "*…not between rival political ideologies but between competing economic models. And with injection of politics into economic decision-making, an entirely different set of winners and losers is emerging*". Similar views were presented by other authors (Luttwak1990, 1999; De Long and Cohen 2010; Rickards 2011; The Economist 2012).

Analysis of state capitalism built upon comparative framework plausibly premises that not only economics matters: state capitalism has a broader agenda and politics looms high on it. "*Leaders of authoritarian governments have embraced the capitalist system not only in order to maximise economic performance in their countries but also with the aim of promoting their political goals and furthering their political dominance*" (Bremmer 2010, 249). Whatever authentic ambitions of the state are, the latter, according to Bremmer, dominates the market for a certain political gain. As the trend expands, ramifications overcome the borders of a nation-state making international politics increasingly prone to frictions and exposing global markets to distortions. Generated this way outcomes in either arena are suboptimal, which is particularity unpopular with the countries preaching free-market principles and especially so in a period they are striving to defeat a severe crisis: "*… state capitalism challenges free-market capitalism conceptually and practically: it offers an attractive alternative to leaders of emerging economies and it distorts capitalism's efficiency, thus undermining future recovery*" (Ibid).

For a number of reasons, the very survival of state capitalism requires the external dimensions. As Dupuy and Truchil (1979) have shown, for instance, state capitalism normally inherits and deepens further a dependency on foreign capital and technology. While this holds true in modern times, too, another substantial consideration is that contemporary state capitalism increasingly needs the external demand for the goods it produces. Often these goods are natural resources, in particular oil and gas.

3. Russia's state capitalism

3.1. Russia's specifics: geography first

Russia is normally referred to as one of the typical representatives of state capitalism. Musacchio and Lazzarini (2012), however, show that Russian SOEs contribute about 20 percent output to total GDP[4], compared with 30 percent in Brazil and China. Also, though higher than in many other state capitalist economies, Russian SOEs' market capitalisation constitutes some 40 percent of the total, while it stands at 70 percent in China (The Economist 2012).

Despite neo-liberal thinking was influential at the outset of economic transition in Russia, national economic policy embraced a peculiar combination of *monopoly, oligarchy and liberalism*. One of the reasons behind was Russia's mode of globalisation. Sakwa observes that Russia was *"involved in a process of mutual interaction with other states and non-state actors. Too often Russia's readiness to adapt to the norms of international society came into conflict with attempts to assert its autonomy and interests in international politics*" (Sakwa 2012: 968). In this connection, it is essential to recollect Russia's overall economic situation in the beginning of the market reforms in the early 1990s. To bring about necessary structural reforms, Russia desperately needed the financial resources. With the oil price at its lowest, becoming a party of the globalisation process was one out of altogether very scant choices enabling Russia's access to the much required means. Faced with domestic economic constraints, Russia was enforced to seek place in the international setting as rule-taker. To a degree, such somewhat quasi-voluntary manner of Russia's involvement in globalisation has generated certain contradictions with the fundamentals of national economic governance and resulted in suboptimal outcomes.

Inward-oriented analysis suggests other explanatory frameworks for the specifics of Russia's economic model. Lynch (2002), for instance, argues that apart from the problem of the Soviet legacy of economic inefficiency and all the deficiencies of contemporary economic governance, there are three major groups of mutually interacting factors of economic geography that sustain the case for the state in Russian economic development. Among those factors, Lynch (2002, 39) defines "*severity of climate, distance (including the growing dislocation between population and natural*

[4] To be objective, the estimates on SOEs' role in Russian economy vary greatly. Bank of Finland, for instance, assesses the SOEs' share in Russia's total GDP at 50 percent noticing that it differintiates between the sectors: from about 50 percent in banking and oil production sectors to over 70 percent in transportation sector (including pipeline transmission). November 23, 2012, http://www.suomenpankki.fi/bofit_en/seuranta/seuranta-aineisto/pages/vw201247_2.aspx.

resources) and predominance of expensive land over cheap water transport". Handling such natural denominators of Russia's inherent economic inefficiency as climate and spatial dimension (rendering into economic measure of cost of production) and resource endowment (positing a dilemma of geologically existing vs. economically available resources) is by far a tremendous task. Lynch's (2002, 45) main argument is that "*Russia as a whole cannot be developed economically without the state*". On the other hand, Lynch (2002, 45) notice that Russia's economic geography does not exclude the possibility for the market economy to develop, but "*the corrupt and criminalised state*" renders the economic system "*not viable over the longer run, because it cannot generate growth and prosperity*". Russia remains captive to a detrimental combination of inherent disadvantages resultant of the country's economic geography and drawbacks borne within its inefficient and corruptible public sector. And yet Lynch (2002, 45) emphasises that "… *it would appear implausible to imagine that even an efficient and incorruptible Russian economy and public sector could thrive under strictly liberal auspices, without a state structure and state policies designed to compensate for the many inherent disadvantages that Russia faces as a result of its economic geography*".

Another strand of research on Russia's state capitalism considers "*… the interactions between economic structures, political processes and social outcomes*" (Buccellato and Mickiewicz 2009, 405). Spatial dimension and resource endowment are analysed as significant determinants informing Russia's economic governance (Bradshaw 2006; Buccellato and Mickiewicz 2009; Gaddy and Ickes 2010). For transition economies in general, the territorial extension was found to be positively correlated with the level of inequality: the larger the extension of a country, the higher the impact of region-specific effects on income distribution. In resource-rich transition economies, government is known for its attempts to institute centralised and powerful rent management system. The effects of the latter are weak entrepreneurship activity and low entry to resource producing sectors, which in turn, lead to significant inter- and even intra-regional income inequalities. Buccellato and Mickiewicz (2009) posit that local economic structures dominated by natural resource rents endowed business elites see the distortion of democratic processes. This process is explained as resulting in state capture, when non-regional actors are able to shape institutions and policies to their advantage through corrupt transactions with public administration and politicians. For that reason, even regions with the largest volumes of oil and gas produced are not guaranteed from higher than national average poverty (Gylfason and Zoega 2002).

In the economic literature, the role of natural resources has been broadly discussed as having impact on economic prosperity, development and long-term growth (Corden and Neary 1982; Eastwood and Venables 1982; Corden 1984; Sachs and Warner 1997; Davis and Tilton 2005; Stern 2010). While positive effects of natural resource endowment on growth are proved (Sala-i-Martin et al. 2004), there are evidences that one-sided hydrocarbon specialisation may eventually cost the national economy serious misfortunes.

The Dutch Disease theory exemplifies how the boom in the hydrocarbon sector may affect negatively the entire economy. High concentration of rents in the hydrocarbon sector, if not accompanied by efficient institutions and government policy, tends to result in a skewed distribution of income (Davis and Tilton 2005). In addition, natural resource abundance may stimulate rent-seeking behaviour that, together with highly concentrated bureaucratic power, induces corruption in the economy and, in turn, impairs further the quality of the governance (Leite and Weidmann 1999; Davis and Tilton 2005).

Although Russia's energy export orientation played a distinct role in softening the consequences of the 2008 crisis (owing to accumulated revenues), it at the time exposed its inadequacy and revealed that its persistence is vicious and risks Russia's long-term economic prospects (Tabata 2009; Gaddy and Ickes 2010). Myant and Drahokoupil (2012) found that the global financial crisis consequences for the Russian economy were more profound than it could have been expected for the energy resource exporter. The Russian economy suffered not only from falling demand (and, hence, shrinking revenues) for oil and gas exports, it also experienced decline across a broad range of industries, including construction, non-manufacturing and, especially, manufacturing sectors. While handling the crisis' hardships, the Russian government was seriously concerned with bailing out the large businesses who turned out to be profoundly dependent on foreign short-term financing. When the tight financial situation coincided with shrinking export revenues, these companies realised their vulnerability in refinancing their liabilities. In such circumstances, the government could not let these companies bearing significant social costs to fail and stepped in spending on salvage, according to some estimates, some $50 billion.

Thus, Russia's economic geography and resource endowment need to be recognised as pivot denominators of the government policy.

3.2. Ideas and norms

"Competitors… it is abroad. Here, there are no competitors; we are all partners."

(Igor Sechin, president of Rosneft, on the rules of the game in the Russian fuel-energy complex, http://www.rusenergy.com/ru/favorites/)

Andrews-Speed (2010) holds that ideas and institutions, together with other factors, can stimulate or constrain policy change. Established ideas (included in embedded informal and formal institutions) take the form of paradigms. When a paradigm demonstrates a failure, new ideas through the process of social learning stimulate policy changes (resulting in adjustment of existing instruments or creation of new instruments, the first and second order policy changes, respectively) or lead to adoption of a new paradigm (the third order policy change).

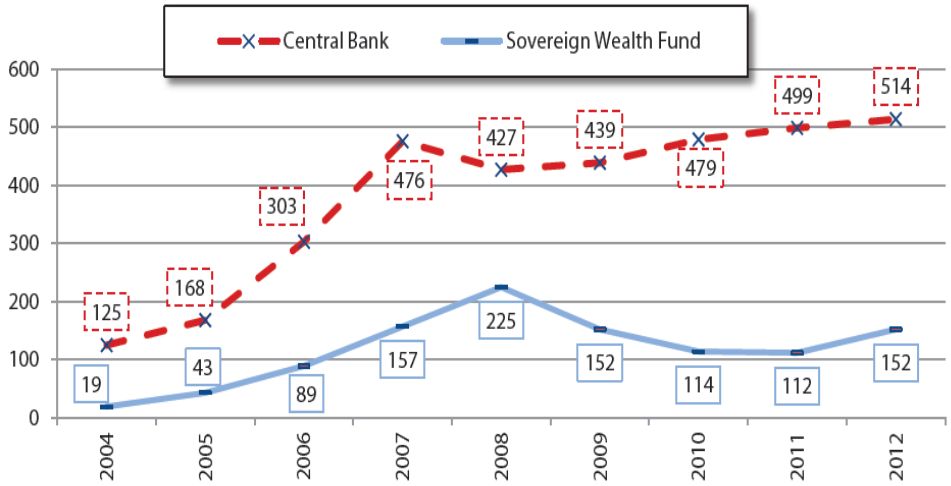
Although it was intended to match the overall course of market reforms, Russian energy policy in the 1990s suffered numerous failures due to continuing Soviet practices. Energy policy was built upon the perception that the energy sector had to further maintain the role of a donor to the entire economy. Russia's energy policy until the 2000s can be seen as rather fragmented and inconsistent with the course of market reforms which had commenced in the early 1990s (Miller 2009). The goals formulated in the programme documents had been poorly achieved, and were consequently dragged over into the next paper on energy policy, only to yet again remain unfulfilled.

By 2004, the overall domestic political environment had shifted towards greater power of the state. From 2000, the oligarchs were ousted from the media and ejected from the State Duma by forcing out the liberal parties that they financed and which were the main conduit for their lobbying. In 2000, the institute of Plenipotentiary Representative of the President of the Russian Federation in a Federal District was established to curb the power of regional governors. Finally, the forced dissolution of Yukos and the redistribution of its assets to state-controlled companies signalled the advent of state capitalism, a system of state entrepreneurship backed by mechanisms of selective support for loyal to the government companies and punitive measures against entities opposing federal power *vertikalj*.

Since 2004, energy policy has been based upon more pronounced role of the government. The state's interests in the gas and oil industries were carefully guarded through nationalisation, resulting in a higher degree of monopolisation, limited presence of foreign capital, sluggish competition in the sector and its chronic overall inefficiency.

This policy mode was emboldened by extremely favourable external conjuncture of oil, gas and other raw materials markets. The oil and gas sectors generated approximately 30 percent of GDP, about 50 percent of budget revenues and earned over 70 percent of the country's foreign currency. These contributions turned Russia into one of the world's largest holder of SWF and foreign exchange reserves (Graph 1).

Graph 1. Russia's sovereign wealth fund and Central Bank reserves (US$ bn)



Source: Russian Analytical Digest No. 113, 15 May 2012,7.

Before 2008, Russia has enjoyed significant economic growth of around 7 percent annually, considerable inflow of foreign investment, substantial rouble's appreciation, large budget surpluses, etc. Importantly, Russian population sensed a remarkable rise in living standards. This made the Russian government believe that the country's economic strength must be matched by its weight in global affairs. The emphasis on economic power as a prerequisite for the national power build-up became particularly evident during the second term of Putin's presidency.

From 2006, the overall landscape for policy-making in Russia was informed by the ideological platform of sovereign democracy proposed by the then Deputy Head of the Presidential Administration Vladislav Surkov. It essentially meant to deter a severe criticism about the violation of the democratic principles in Russia and proclaim that Russia has its own understanding of democracy. The concept was critiqued both domestically and internationally for its conceptual flaws, inconsistency and ambiguity.[5]

In 2008, the pendulum of economic fortune has swung away from Russia. Following collapse of oil prices and amid the global recession, Russian oil and gas production

[5] For more detail see, for instance, Okara, Andrei (2007) Sovereign democracy: A new Russian idea or a PR project? Russia in Global Affairs, Vol. 5, No. 3, July – September. pp. 8-20.

and exports declined adding to economic downturn. In 2009, Russia's GDP contracted by 7.9 percent with industrial production declined by 9.3 percent, exports slumped by 35.8 percent, imports dropped by 34.4 percent and FDI toppled by 50.1 percent. In such circumstances, concerned with the ways to support the energy sector itself, the government started amending the tax and customs policy, as well as considering incentives to activate investment (including foreign) into long-term large scale and risky projects.

Faced with the constraints imposed by resource dependency (resource addiction, in words by Gaddy and Ickes 2010), the Russian government activated the search for a qualitatively new pattern for economic development. The then President Medvedev emphasised these ideas in the Long Term Concept for Social and Economic Development of the Russian Federation until 2020, in his article "*Go, Russia!*" and in his 2009 Presidential Address to the Federal Assembly of the Russian Federation. That was how the modernisation agenda became an official policy course with especially established institute – The Presidential Commission for the Modernization and Technological Development of the Russian Federation.

In June 2009, in his speech before the Commission, Medvedev formulated five target areas for the technological breakthrough, naming energy efficiency and energy saving (including the development of new energy sources) and nuclear technology among those core fields. Practically, a tremendous financial support has been funnelled into almost sole innovation project - Skolkovo.

To buttress the then President's Medvedev modernisation strategy, a new ideological platform was presented by the United Russia in 2009. It was dubbed conservative modernisation. While socio-economic advantages of such a conception remained rather dubious, the political dividend was more identifiable: the government apparently has opted for pursuing a policy of petite temporary improvements of the traditional economic structure in order to preserve the existing all too fragile and negligible socio-economic comfort. The history of economic development evidences that large-scale modernisation entails certain risks of the loss of legitimacy for the government (Moe 2010). This seems to be one of the credible explanations of the Russian government's inclination toward a version of exclave modernisation.

4. Russia's state capitalism and energy sector

Recently, Russia has been either the world's largest or the 2nd large (after Saudi Arabia in oil and the USA in gas) producer and exporter of oil and gas. During the pre-2008 bonanza, Russia accumulated the world's 3rd largest foreign exchange reserves and the 7th largest sovereign wealth fund.

Russian energy studies conventionally scrutinise energy as Russia's foreign policy trump card. This appears to be a simplistic interpretation. There has always been an understanding (or, recalling Putin's dissertation,[6] could well be even a plan) that energy is one of the most crucial elements of Russia's economic power. Even a cursory perusal of Putin's thesis[7] helps identify the elements of what later on became the core elements of Russia`s economic strategy. Throughout the 2000s, the Russian energy policy was developed upon the notion that blessed by endowment of various natural resources Russia possesses a unique potential, which if rationally exploited can boost the country's economic development and reinforce its political power.

4.1. Energy policy making and implementation

"You cannot draw the boundary, as it was in 1917: this is red, this is white. We all work for the country's sake, because the major share of revenues goes to the state"

(Vagit Alekpyorov, president of Lukoil, on the state policy in oil industry, http://www.rusenergy.com/ru/favorites/)

Following a dramatic change in the global energy market after 2008, the government was forced to revise Russia's energy policy. In 2009, Energy Strategy of Russia for the period up to 2030 (hereinafter, Strategy) was adopted.

In the Strategy, the government emphasised a new approach, according to which it is not the world oil price but the tempo of domestic economy's recovery that defines the key parameters of the Strategy's two scenarios. The first scenario envisaged quick economic revival with the consequences of the downturn tackled before 2015. In turn, the second scenario envisioned a slower pace of overcoming the repercussions of the crisis, with full recovery expected by 2020/2022.

The Strategy outlined three phases. A substantial overhaul of the Fuel Energy Complex

[6] Seeking a Candidate of Sciences degree in Economics with specialisation in National Economy Planning and Management, defended at Saint Petersburg Mining Institute in 1997.
[7] Translated into English excerpts are available in Balzer, H. (2006) Vladimir Putin's Academic Writings and Russian Natural Resource Policy. *Problems of Post-Communism.* 53.1. 48-54; and Balzer, H. (2005) The Putin Thesis and Russian Energy Policy. *Post-Soviet Affairs*. 21.3. 210-225.

(FEC) to become an additional engine pushing the domestic economy towards post-crisis recovery would be a task at the first stage (2013–2015). During the second phase (2016–2020/2022), an array of cutting-edge innovations and technologies would be introduced; greenfields would become operational and significantly expand the sector's production and export capacity. In the period 2021/2023–2030, considerably improved energy efficiency coupled with the enhanced use of non fossil fuel energy sources (nuclear, solar, wind and so on) would boost Russia's robust economic development. The Strategy pursues an array of aims across four major dimensions: energy security; the energy efficiency of the domestic economy; the economic efficiency of the FEC and, the ecological security of FEC.

The Strategy saliently identified new geographical dimensions for the diversification of Russian exports. It specifically envisages the accelerated development of new oil and gas deposits in East Siberia, the Far East, on the Yamal peninsula and on the Arctic shelf. Accordingly, export flows are projected to switch from the West to about 63 percent for oil and 56 percent for gas (from 2005 over 80 percent and over 60 percent, respectively) more towards the East to over 20 percent in oil and gas (from 2005 about 5 percent and zero for oil and gas, respectively).

In 2011, a number of other important program documents were adopted, among which there were the General Scheme of the Oil Industry Development until 2020 and the General Scheme of the Gas Industry Development until 2030. These documents were synchronised with the provisions of the Energy Strategy 2030. The Oil Strategy was additionally coordinated with the Transport Strategy until 2030. The Gas Strategy was developed as one of the steps toward the implementation of The Complex of Measures on the Hydrocarbon Pipeline Transport Development (2004). The Gas Strategy was also linked to the Strategy of Development of the Key Industries until 2015 and the Program of Creation of Unified System of Gas Production, Transportation and Supplies in East Siberia and the Far East with Possibility of Exporting Gas to China and other Asia-Pacific Countries (Eastern Gas Program, 2007).[8]

On the international arena, Russia remained resolute to participate in the process of founding of new global energy governance as a rule-maker. The idea proposed in April 2009 by former President Medvedev for a Conceptual Approach to the New Legal

[8] Approved by the government on June 15, 2007, by the Ministry of Industry and Energy on September 3, 2007, Order # 340, http://bestpravo.ru/rossijskoje/rx-normy/r9n.htm. As of November 2012, the Program is under revision.

Framework for Energy Co-operation[9] has later on been reiterated by the Minister of Foreign Affairs. Sergey Lavrov articulated that "*…sustainable development requires reliable supply of energy resources for the global economy. Russia has made a proposal to elaborate a Convention on International Energy Security that would cover all aspects of global energy cooperation taking into account the balance of interests of all actors in the international market. We call for starting practical preparation of this document.*" [10]

As far as energy policy concerned, the government has a variety of policy instruments. These can be broadly divided into administrative (of direct influence and control) and economic (of soft governing power), balance between them shifts over time depending on the priorities the government sets both domestically and internationally.

As the following overview of the Russian energy policy presents, the government attempts to find optimal solutions to the specific features of the Russian economy we early identified.

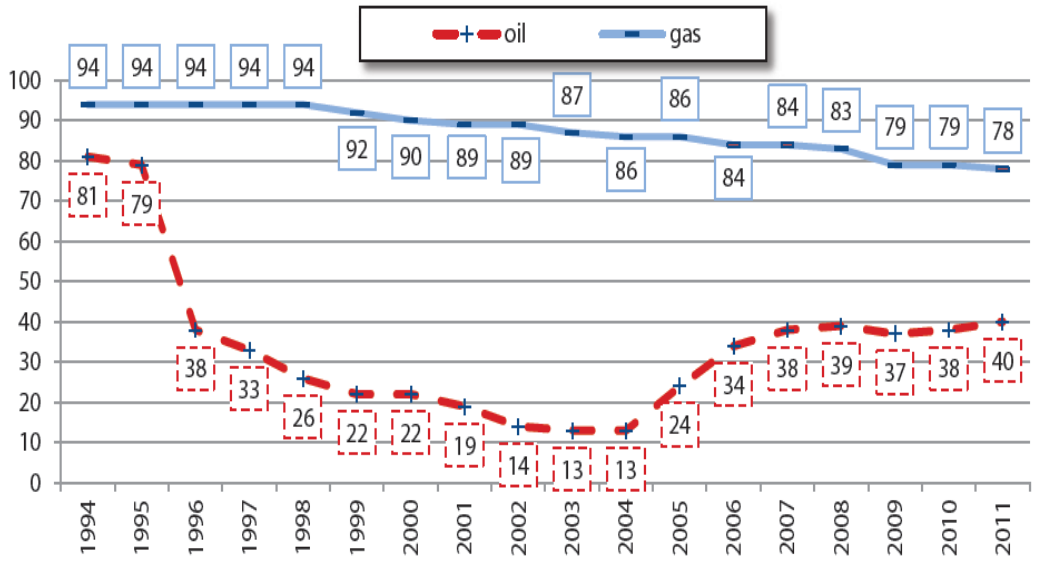
Decision-making: In addition to the legally established division of authority between the president and the prime minister, the ministries in charge of energy, financial and economic development, there are many other perspectives of the state vs. business relationships when regards the energy policy making (Hanson and Teague 2005; Adachi 2010; Shadrina, 2010a, 2010b). One particular arrangement enabling direct involvement of the state in the energy sector - a system of the government official representatives in the BoDs' of major oil and gas companies[11] - was expected to be terminated in the spirit of the then President Medvedev's 2011 initiative. The latter was meant to exclude the ministers and other officials from the boards of directors of SOEs. However, the newly elected President Putin made clear that although the government's role in the sector is transforming, it does not necessarily signify a more independent decision making by SOEs, neither does it promise a more transparent business environment. Quite the opposite, set up in June 2012 the Commission on Strategic Development of Energy and Environmental Safety [12] (hereinafter, the Energy

[9] http://archive.kremlin.ru/eng/text/docs/2009/04/215305.shtml
[10] Statement by H.E. Mr. Sergey V. Lavrov, Minister of Foreign Affairs of the Russian Federation, at the 66th Session of the UN General Assembly, September 27, 2011, *http://www.rusmission.org/policy/36*
[11] In 2010 the federal government's officials were represented on the companies' BoDs as follows: Gazprom – First Deputy Prime Minister (chairman), Minister of Industry and Trade, Minister of Economic Development, Special Representative of President for International Cooperation; Rosneft - Deputy Prime Minister (chairman), Head of the Federal Agency for State Property Management; Transneft – Minister of Energy (chairman); Zarubezhneft - Minister of Energy (chairman); RZD – Deputy Prime Minister (chairman).
[12] See more http://www.rusmininfo.com/news/2012-03-21/russian-government-recommends-9-

Commission) altered the overall principles of the economic governance in Russia. The President appointed himself as Chairman of the Energy Commission and Sechin, Rosneft's CEO from 2012, as executive secretary. The Energy Commission challenges the government's control over the energy sector, as it has extensive mandate embracing tariff, tax and price policy for oil, petrochemicals, gas and electricity and investment, all of which becomes of binding power for other authorities. This effectively means that significantly less financial resources are left at the government's disposal. Prime Minister Medvedev defends his earlier expressed visions on the sector's privatisation and the government's withdrawal from the SOEs by 2016, but finds no solid support.

Sector's structure: State-owned companies (SOCs) play an important role in all segments of the Russian FEC: exploration, development (Graph 2), processing, transportation/ distribution, marketing, etc. (Shadrina, 2010a).

Graph 2. Share of SOEs in Russia's oil and gas production (%)



Source: Russian Analytical Digest No. 113, 15 May 2012, p.7.

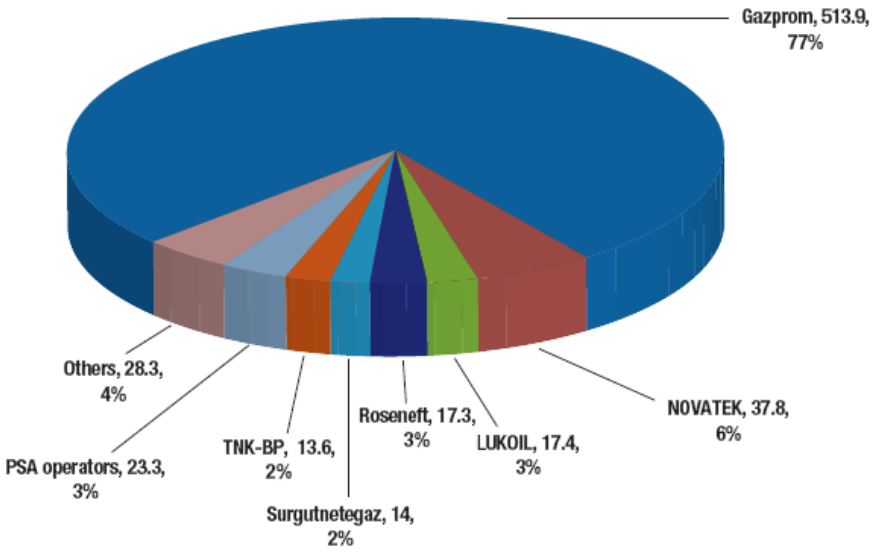
Russian gas sector is represented by natural monopoly Gazprom (state owns 51 percent) and private companies (NOVATEK, ITERA and oil producers: Surgutneftegaz, Lukoil, Rosneft, TNK-BP) (Graph 3). Despite the sector's regulation overtly favours the monopolist,[13] independent gas producers managed to increase their share in total gas

candidates-board-directors-rosneft-list-does-not-inc, http://www.europeanenergyreview.eu/site/pagina.php?email=pkdriessen@gmail.com&id_mailing=318&toegang=432aca3a1e345e339f35a30c8f65edce&id=3899

[13] See, for example, The Federal Law on Gas Export. No.117. 2006.

production to 21.8 percent in 2010 (against 9.5 percent in 2000).

Graph 3. Natural gas production in Russia in 2010 by company (bcm, % of the total production)



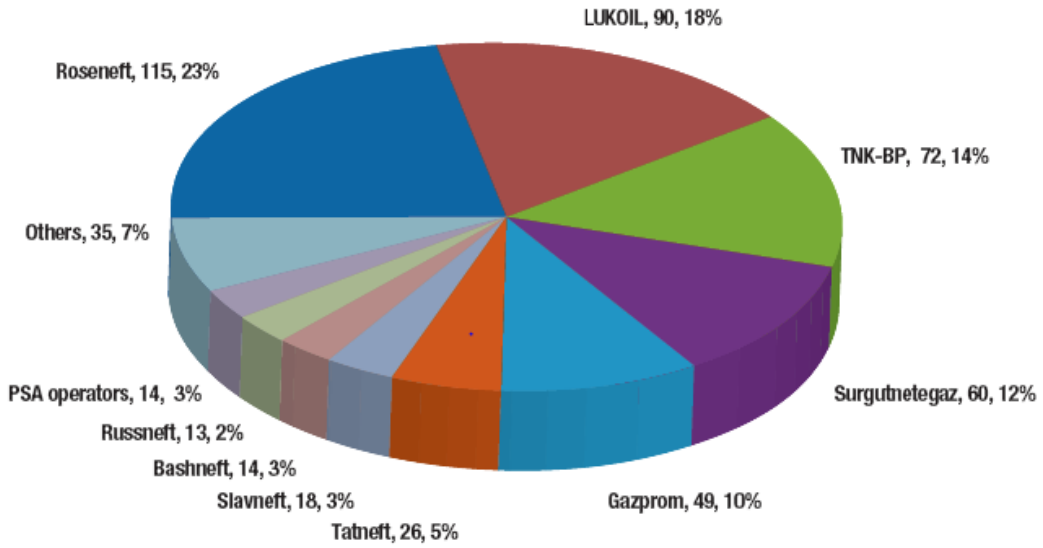
Source: http://www.iisd.org/gsi/sites/default/files/ffs_awc_russia_eng.pdf

In the oil sector, there are eight vertically integrated companies with their 145 subsidiaries and many midsize companies (bringing the total number of oil-producing companies to 325, as of 2011). *Rosneft* (state holds 75.16 percent through OJSC Rosneftegaz) stood out as Russia's largest oil producing company following the purchase of Yukos' assets in 2007 and is to become by far the world's largest oil producer after the agreed in 2012 deal with TNK-BP is finalised[14] (Graph 4). Rosneft's deal with TNK-BP is expected to raise the overall share of SOEs' in Russian oil production to over 50 percent.[15]

[14] As revealed October 22, 2012, there is a two-part deal between Rosneft and TNK-BP. In the first part, Rosneft is acquiring BP's 50 percent stake of the joint venture in exchange for cash and Rosneft's stock worth $27 bn. The deal will give BP a 19.75 percent stake in Rosneft. In stage two, AAR would get $28 bn in cash for its half, though this deal is not yet finalised. The deal is worth some $56 bn and stands to be the largest in the industry since Exxon bought Mobil in 1999. Materialised it be, Rosneft's daily production is projected to increase to some 4.5 mn barrels per day, allowing Rosneft to take over ExxonMobil.

[15] Reuters, January 2, 2013, http://au.news.yahoo.com/thewest/a/-/world/15751976/rosneft-leads-russian-oil-output-to-new-high/

Graph 4. Crude oil production in Russia in 2010 by company (million tonnes, % of the total production)



Source: http://www.iisd.org/gsi/sites/default/files/ffs_awc_russia_eng.pdf

By a criterion of favourability of the regulative environment, Rosneft can be seen as being granted as privileged status as Gazprom is in the gas sector. With the former Deputy Prime Minister and President Putin's long-time loyal aide Igor Sechin becoming the head of Rosneft, the company's favourability factor is by all accounts only to rise.

In the transport segment of the oil and gas industry, rail and marine transport play very important roles. The rail transport, represented by Russian Railways (RZD), a 100 percent state-owned monopoly, played an important role in Russia's oil exports to China before 2010, until the ESPO's China-directed leg became operational. RZD expands its interests elsewhere acquiring assets in the ports all across Russia (Far East, Ust Luga, Novorossiysk, Murmansk, etc.). The marine transport has somehow regained its attractiveness after the Sakhalin LNG plant came online and other possible projects in the Russian Far East went into the negotiation stage.

The trunk pipelines, however, play by far crucial role in Russia's gas and oil exports. Gas and oil transportation, dominated by Gazprom and Transneft, respectively, are monopolised. While it is often argued that this is the only mechanism of effective state regulation possible, the fallouts of this system can be clearly comprehended: the timing and direction of export routes affect the private companies' production targets and exploration choices. The number of privately-owned pipelines remains very scant: Lukoil, Shell (the gas pipeline within Sakhalin II), and TNK-BP (the gas pipeline in Kovykta).

Transneft is a state-owned intermediary company specialising on transport services in oil exports. The company concentrates on primarily export operations, and increasingly, in particular, in the Far East and Eastern Siberia, on pipeline construction. Transneft's monopolistic status grants it all the benefits from transportation of Russian oil through the system of trunk pipelines across Russia.

With regard to exploration, in the circumstances of falling or levelling-off outputs, the state became concerned with the speed the depleting gas and oil fields are being replaced by the new discoveries. It is against this backdrop that the government decided to bring more control into geological exploration and founded Rosgeologiya in 2011.

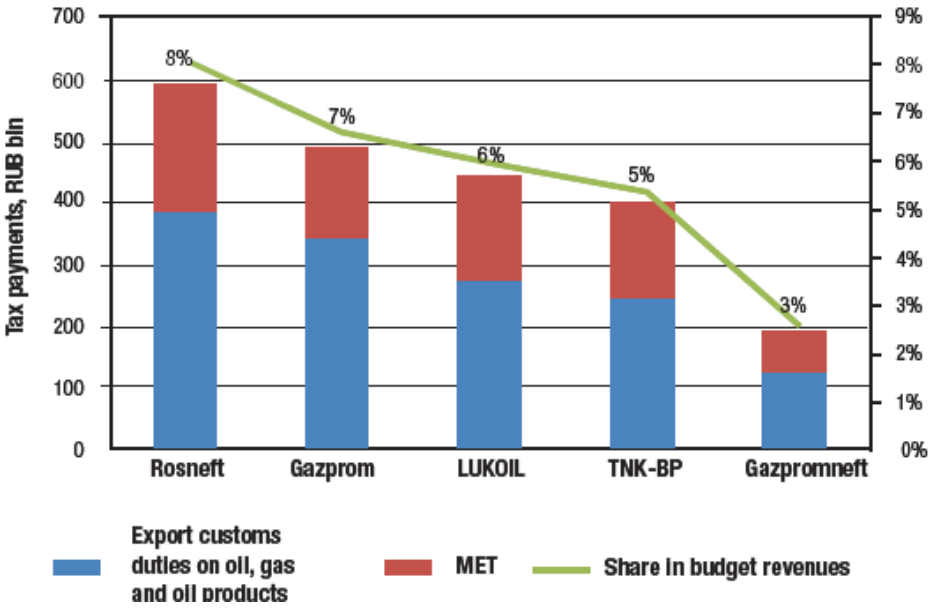
Thus, SOCs are the principal actors in the Russian oil and gas sector. Competition in industry is limited allowing the survival of SOCs despite their rather low economic efficiency. As Hanson and Teague (2005) and especially Adachi (2010) show, although to a lesser extent than until the early 2000s, yet big businesses try to exploit imperfect regulatory framework to their own benefits developing various specific managerial practices,[16] which have wide-ranging negative impacts on the energy industry and Russian economy as a whole. Increasingly however, in order to be allowed to operate in the sector the SOEs and large private companies need to enter into one or another sort of collusion with the state.

The modern structure of Russian oil and gas sector is the result of privatisation of the 1990s and re-nationalisation after 2004. The latter was arguably an interim phase to help change the owners. Recently, the idea of 're-privatisation' has become a popular topic for heated discussions about the future transitions in the sector.

Taxation of production and exports: Recently, approximately 50 percent of the budget revenues were contributed by the oil and gas revenues with the oil industry generating nearly 90 percent of the sectors' total revenues (Graph 5).

[16] Adachi (2010) provides excellent analysis of informal corporate governance practices, ICGP, in Russia such as limiting 'undesirable' shareholders, share dilution, transfer pricing, asset stripping, non-transparent ownership and 'bankruptcy to order'.

Graph 5. Payments of the mineral extraction tax and export duty to the federal budget by major oil and gas producers, 2009



Source: http://www.iisd.org/gsi/sites/default/files/ffs_awc_russia_eng.pdf

Russia has a three-tiered tax system: a corporate tax, a mineral extraction tax (MET) and the export duties on crude oil and petroleum products. The corporate tax is imposed on profit at a rate of 20 percent (equal to that in other industries). MET was introduced in the 2002 tax reform, replacing the levies and taxes that were previously imposed on subsoil asset developers. In the oil sector, MET and export duties are linked to oil price and the correlation is progressive: the higher price the higher levy. As for the gas, the MET is fixed and the export duty is defined in an ad valorem form. A general note can be made that oil sector is under a heavier tax burden. By some 2011 estimates, export duties and MET were totalling to 30 percent of gas price, while reaching 60-65 percent level when compared to the oil price. This situation is, however, may somewhat change, because the government implements a number of adjustments in the area of taxation of gas. For instance, the MET for Gazprom is to be increased gradually over the next several years, while the independent producers will continue paying the MET at a discounted rate. [17]

The oil sector's production stagnation prompted the government to introduce some minor tax cuts, returning the industry to modest growth in 2009. Besides raising the taxable threshold according to which the MET was applied, in 2008 the government

[17] RusEnergy. November 29, 2012 http://www.rusenergy.com/ru/news/news.php?id=63521

also modified the oil export tariff-setting system, reducing the period between the point of monitoring of price and point of adjustment of tariff from two to one month. The moderate success of these initiatives in resuscitating the sector in 2009 has spurred calls from the domestic oil industry for more tax breaks and incentives, including a shift to profit-based taxation and a change in the methodology in determining oil export tariffs.

Launched from January 2007 tax exemptions on oil production and exports from Eastern Siberia have helped provide incentives for producers operating in the region. Rosneft, Surgutneftegaz, and TNK-BP were highly satisfied with the tax breaks, but the Ministry of Finance (MoF) strongly opposed such a system noting that East Siberian tax holidays result in losses of budget revenues of some 120 billion roubles (approximately 3 bn euros) annually. Eventually, the regulations for the eastern provinces were set with a provision that they are to be gradually terminated by 2013. Recent amendments to the respective documents prove that preferential regime will be extended. Moreover, gas production in East Siberia and the Far East will also be put under preferential treatment with the MET holidays provisioned for the new projects during 25 years.

The shape of taxation system has been a product of the debates among three government entities: the Ministry of Economic Development, the MoF and the Ministry of Energy (MoE). The conflict of interests here is obvious. While the MoE's utmost concern is to modify taxation so that it would enable an increase or at least stabilisation of the production, the MoF most of all cares about the budget revenues.

Another novelty in the area of export tariff regulation will be enacted from 2013. According to the amendments to the Law on Customs Tariff, export duty will vary depending on the chemical parameters of oil and the area of extraction. In this manner the government, in particular, intends to support the development of low-margin greenfields located in remote zones with severe climatic conditions (the Far East, Russia's sections of the Caspian Sea and Russia's continental shelf) and deposits of tight oil which has higher production costs and lower parameters of commercial attractiveness.

Speaking of the government's effort to improve the structure of energy exports, from October 1, 2011, a new system of export duties (coined "60-66") was enacted. Under this regulation, set through the end of 2014, the marginal export tax on crude oil is reduced from 65 percent to 60 percent, while light and heavy petro products are to be levied at a unified rate of 66 percent and gasoline – of 90 percent of the tax on crude

oil. The logic behind this novelty was apparent: the government attempted to terminate export of low processed oil products (perceived as a hidden form of subsidisation of foreign refineries using these low-quality Russian products as a feedstock) and stimulate the upgrading of Russian refineries. However, available provisional data evidence that there is no particular shift taking place in a desired direction.[18]

Investment: In the aftermath of the 2008 crisis, investment in Russian energy sector has become a matter of vital importance. Estimates on the investment needed in the sector range significantly. In 2008, for instance, the Ministry of Energy referred to a level of $240 billion needed through 2020, while the IEA evaluated the need as up to $400 billion by 2030. The Strategy 2030 assessed the investment required for oil and gas industries through 2030 as of over $1100-1200 billion. The Strategy envisaged that the lion's share of investment, up to 80 percent, would come from the private sector under so called public-private partnership scheme.

Recently, the Russian government seemed to be inclined to permit more active FDI involvement. In Russia, as it is known, the attitude toward non-residents in the oil and gas sectors has changed several times – from a romantic period of PSA and active invitation to the sector to a tough period of severe resource nationalism that resulted in a law forbidding foreign investment into Russian commercial organisations of 'strategic importance'. After 2004 the Russian state control has been growing. The sector was traditionally steered via tax incentives, export regimes, pipeline access, oil and gas fields' auctions and tenders, etc. In July 2008, a number of amendments of the federal laws - On Continental Shelf, On Gas Supply, On Subsoil – resulted in assigning Gazprom and Rosneft the roles of the government agents in oil and gas sector, while foreign businesses found themselves under tougher regulation. Russia was severely criticised for such a move.

Additionally, in 2008 the Strategic Sectors Law listed 42 types of activity of strategic significance, stating that foreign investment in these areas should either be totally restricted or subject to approval on a case-by-case basis. The Law introduced the category of 'subsoil blocks of strategic significance', and envisioned rather complicated licensing procedure by a number of agencies, including the Federal Security Service (FSB), the Ministry of Defence, the Ministry of Economic Development, and the Ministry of Energy. Apparently, the Law has further fortified Russian oil and gas sector from foreign 'invasion'.

[18] Vedomosti. September 7, 2012, http://www.vedomosti.ru/companies/news/3683441/mazutu_stavka_ne_pomeha; RusEnergy November 27, 2012 http://www.rusenergy.com/ru/news/news.php?id=63470.

After 2008, many Russian energy companies opted for the suspension or even termination of some of their investment programs. Seeking the means to ensure the sector's development, the government has initiated some stimuli. The investment into the ESPO oil pipeline were backed through wounding down the export duties on oil extracted from a number of deposits in East Siberia. Also, the government introduced tax exemption for the first 10 years of production or first 25 million tonnes of crude oil produced (whichever occurs first) in East Siberia, for the first 10 years of production or 35 million tonnes of crude oil produced for the Arctic continental shelf, 10 years or 20 million tonnes – for the offshore deposits in the Black Sea, and 10 and 30 – for the Okhotsk Sea, all under the condition for period of geological prospecting during up to 10 years and commercial exploitation during up to 15 years.

As for the production sharing agreement (PSA) as a form allowing foreign investment, back in 2003 Russia decided to stop issuing PSAs for the new projects. In 2006, the government pressured the Sakhalin II consortium prompting the foreign companies operating the project under the PSA to sell control of the project to Gazprom. The reasoning was to obtain the easier control over the costs, ensure more of the revenues from the project, and have a say in the project's export marketing strategy, not lastly, do not let the consortium's China-oriented export plans materialise.

At some point, it seemed that financially constrained government was seriously considering the abolishment of the restrictions on investment by the foreign and Russian private companies in the strategic deposits and offshore blocks. Nonetheless, there was no particular improvement of the investment climate for the foreign investors in Russian oil and gas sector. The majority of licences are held by Gazprom and Rosneft and the Federal Subsoil Resources Management Agency's officials admit that should 14 of the remaining undistributed licences be given to these two, Russia can safely forget about the offshore deposits development. Impartially speaking, the SOEs are technically and technologically incapable of implementing the offshore deposits, but as long as the competition is inhibited, neither private no foreign capital can enter the sector and boost its development. Currently, every deal of significance with the foreign energy companies is virtually being authorised by the President himself. Even though Rosneft has managed to conclude the deals with several foreign energy companies (ExxonMobil, Eni, Statoil[19] and TNK-BP[20]), with especially remarkable progress seen

[19] For more detail see: http://www.osw.waw.pl/en/publikacje/osw-commentary/2012-05-09/natural-resources-russian-continental-shelf-foreign-investors-s
[20] For more detail see: http://www.bloomberg.com/news/2012-10-22/rosneft-to-buy-tnk-bp-for-55-billion-in-third-biggest-oil-deal.html

over the months following Sechin's appointment in May 2012, this does not stand to testify that Russian energy sector has gained more attraction in the eyes of the foreign investors. Rather, there are examples of foreign companies pulling out from (Statoil) or mulling over (Total) the early agreed offshore projects with Gazprom (Shtokman, in particular).[21] This is the real state of affairs, which the Ministry of Energy and Natural Resource seeking about $500 billion of investment for the development of the Arctic shelf in the period to 2050, needs to be concerned about.

Tariff system: Trunk pipelines and railways enable the shipment of oil and gas both across the country and abroad. When it comes to the pipeline system, the major actors here are Transneft and Gazprom, while the rail sector is dominated by RZD. The state control is mainly executed through the setting of prices (tariffs) for transport services and distribution of rights on the access to the pipeline system (including export facilities).

In the pipeline system, the Federal Tariff Service of the Russian Federation (FTS) is the only authority assigned with defining the tariff level for transporting of natural gas, crude oil and petroleum products through oil and gas pipelines. The system of tariff regulation is designed in a two-tiered pattern comprising external (tariffs determined by the state, i.e., FTS) and internal (based on decisions adopted by the state representatives on the company' board of directors) control. There is a variety of tariffs charged domestically. But tariff and transit fee are by no means less crucial aspects of Russia's external energy ties: the tariffs and fees often become a subject for tough intergovernmental negotiations.

The economics of pipelines is often affected by politically-motivated decisions. One of the examples of the kind is the East Siberia – Pacific Ocean pipeline (ESPO) tariff. The pipeline was built upon the government's decision to move ahead with the implementation of Russia's Asian energy strategy. Exceptionally harsh geological and climatic conditions (mountains, rivers, tundra, permafrost, etc.) and almost no infrastructure in place prior to the construction resulted in the mammoth costs of the ESPO. With the ESPO becoming operational, a 'catch-22' situation emerged. The actual costs for operating the ESPO trunk estimated by Transneft stood at about $130/t. For the oil producers, that was certainly the prohibiting heights. Eventually, the tariff was set at $50/t with the gap to be bridged through the mechanism of a 'network tariff rate', whereby all users of Transneft's pipeline network - regardless of the area of their operation - are compensating this difference (to Transneft) sharing this way the

[21] For more detail see: http://www.atimes.com/atimes/Central_Asia/NH14Ag02.html

burden among themselves.

Licensing: The government seeks to achieve several tasks through the mechanism of licensing, such as to develop new oil and gas fields and maintain/increase production; to regulate the number of agents and control their qualitative profile; to balance the geographical structure of energy resources development and production; and not least, to receive a certain amount of revenue.

There are exploration and production licenses, which are awarded through either tender or auction mechanisms. If oil is discovered, production license is issued without a tender to a holder of an exploration license. However, before a subsoil user can start to develop the deposit under the license, there needs to be an approval from the authorised body. The subsoil licenses become effective upon their registration with the Federal Subsoil Resources Management Agency (the Agency).

Since January 2005, tenders and auctions are conducted by the Agency (or its regional departments). From 2008, higher uncertainties and the companies' worsened financial capabilities have decreased the overall interest to obtaining subsoil licensees. That is to say, in 2009, 119 auctions and 5 tenders were announced, of which 80 and 0, respectively, were successfully held. Auctions on the subsoil sites located in East Siberia and the Far East were of particularly low success rate: out of over 30 auctions announced only 10 were actually held. This situation resulted in a specific method of the licenses' allocation – the direct transfer of licenses at a minimum price upon the government's resolution – was put into practice. Such, for instance, were the cases of licenses on geological exploration, development and production of the Sakhalin III blocks and West Kamchatka's shelf deposits granted to Gazprom in 2009. The system of licensing obviously contradicts the policy task to boost the explorative activity. Under the current regulation, Russian majors already awarded vast unexplored territories, have no interest in paying lump sums for the rights on exploration and development of the green fields. On the other hand, smaller energy companies often have no sufficient financial resources to bid at the auctions, or relinquish even the application foreseeing future problems with the access to the infrastructure controlled by Gazprom and Transneft. There is an estimate that if the current tempo of geological exploration and development kept unchanged, 150 years would be needed to achieve the targets of the Program for Development of Hydrocarbon Resources on the Shelf of the Russian Federation until 2030.

With seemingly all the necessary elements of energy policy in place, it is tempting to ask what the policy implementation results are. From the very outset of market reforms

in the early 1990s, the Russian government has been persistently formulating the goal of liberating the Russian economy from a disgraceful rank of 'resource appendage', but it appears to have failed to introduce the adequate instruments. Quite certainly, some of the policy changes were prompted by the 2008 crisis, which highlighted the sector's extreme dependence on the external demand for oil and gas coupled with its heavy dependence on the foreign capital and exposed the entire economy's profound addiction to energy rents. Set forth by the former President Medvedev course to modernisation left the most important segment of the Russian economy almost untouched. Modernisation policy has gained its fame for being conservative and limited to almost sole exclave – innovation centre Skolkovo – budded in Moscow region. The signals of the policy's fatigue are accumulating, but generated responses seem to be more capable of sub-optimal adjustments preserving unchanged the energy sector's most obsolete features and retaining the energy policy's most notorious practices.

4.2. State capitalism and the Far East

"Even if the state receives no single rouble from the eastern energy projects, but the region will see an increase in jobs, production of raw materials and higher living standards, it is yet a victory"

(Alexey Kontorovich, Academic, Director of the Institute of Petroleum Geology, Russian Academy of Sciences, on economic policy in the Russian mining sector, http://www.rusenergy.com/ru/favorites/)

Common perception is that the Russian government has so far succeeded neither in utilising the potential (rich natural resource) of the Russian Far East for the integration with the Asia Pacific nor in boosting the development of the region's economy (Khurt 2012). Even a cursory examination of statistics reflects a serious situation: the Far East faces progressing de-industrialisation and de-socialisation.[22]

But whether indeed the government was in earnest pursuing these two goals? In our opinion, it was not. From these two, the idea of integration was more frequently addressed in the policy papers, but it was more a declaration of intentions without concrete steps undertaken to master the way toward this goal. As far as the economic development of the Russian Far East is concerned, the government was not present here in any meaningful mode since the beginning of the radical market transformations. Where are the things now? The two goals seem to be back on the government agenda and out of these two, the revitalisation of the Russian Far East appears to be

[22] Barabanov, Oleg (2012) Problems of Siberia and the Russian Far East. The Valdai Discussion Club. September 4, http://valdaiclub.com/economy/48480.html

prioritised. Where should the things be? The goals of development and integration need to be understood as a dual goal, absence of one does not permit existence of another.

Occupying 36.3 percent of the Russian territory, the Far East contributes only 4.2 percent to GDP, as of 2011, which is a drop against 6.4 percent back in 1998. Moreover, the economic activity is concentrated in four (out of nine) territories which generate 80 percent of Gross Regional Product (GRP). Primorsky krai leads with some 21.7 percent share in GRP, the others are Sakhalin oblast -20.6 percent, the Sakha (Yakutiya) Republic -19.4 percent and Khabarovsky krai adding 18.2 percent, all as of 2010. The composition of GRP reveals that the main sector is extraction of raw materials with some 24.6 percent contribution to GRP, followed by transport - 12.7 percent and construction – 11.6 percent. Manufacturing sector generates only about mere 6 percent of GRP (while public administration is accounted for 7.4 percent).

It used to be a strong belief in the rest of the USSR that the Far Easterners are enjoying higher living standards (and it held to a degree true). Contemporary statistics adjusted for a higher price level, however, advises otherwise: a typical Far Easterner's income is estimated at some 87 percent of Russia's average. This to a certain extent explains the dynamics of the population in the Far East. Since the beginning of the market reforms, emigration and natural loss together lessened the RFE's population by more than 1.5 million people (or by 20 percent when compared to the late 1980s) bringing the number of inhabitants to slightly under 6.3 million people or 4.4 percent of the total Russian population.[23]

Historically, even prior to the outset of the Soviet era, the Far East has been a territory development of which was stipulated not purely by the economic considerations. Depending on domestic and international environment, strategic geopolitical calculus (as primary or secondary order parameter) shaped the contours of the government's supervision over the region.

Going back in modern history of economic development of the Far East, a somewhat cyclical nature of the government policy here can be identified. Every 10 to 20 years, the region has seen a change of development concept reflecting the shifts along the 'goal – resource' node. Minakir (2012) describes nine cycles in the government's economic policy in the Far East, each of which fits in one of the patterns: 'region's goals – region's resources', 'government's goals – government's resources', 'region's

[23] The data was obtained from various sources, mainly news releases; some of the indicators are calculated by the author.

goals – government's resources', 'government's goals – region's resources'. Most frequently employed was 'the government's goals - the government's resources' pattern.

Traditionally, government policy in the Russian Far East has been conducted upon a target-oriented approach. Still in the implementation, the federal (purpose-oriented) program (*federal'naya tselevaya programma*) for Siberia and the Russian Far East development [24] reveals the drawbacks that most of the previously attempted government's programs have also had. The fact that the Program was launched in 1996 (means developed even earlier) explains its somewhat follow-up character. Totally different economic conditions shaped after the economic integration across the territories ended – the immediate consequence of the dissolution of the USSR – were hardly taken into account by the programmers. A number of amendments in the subsequent years have not particularly improved the quality of the document. Furthermore, chronic underfunding of the projects included in the program combined with poor coordination of the resources designated for the projects located in different regions have made the situation even worse.

In the beginning of the 21st century, geo-political considerations seem to have become more pronounced. The region's significance was repeatedly emphasised with regard to two specific areas: transport infrastructure and natural resources, first of all, energy resources. [25] Embracing these ideas vision received the name of "*transnational resource transit developmental concept*" (Minakir 2012, 7).

Before his official inauguration in 2012, president-elect Vladimir Putin stated that in the next 10-15 years Eastern Siberia and the Far East will develop faster than other regions of Russia, describing such development as the most important geopolitical task for Russia.[26] Apparently bearing geopolitical considerations in mind, the government has focused on a stronger transportation ties between the European Russia and the eastern regions. To this end, there are suggestions of prioritising the development of railways in Siberia and the Far East, notably, of the Trans-Siberian Railway and the Baikal-Amur Railway (BAM). Needless to say, a very close attention was attached to

[24] The Federal Program "Economic and Social development of the Far East and Transbaikal Region for the Period up to 2013". Adopted by Resolution of the Government of the Russian Federation on April 15, 1996 No. 480, http://www.economy.gov.ru/minec/activity/sections/econreg/investproject/doc2010011212

[25] "Strategy for Social and Economic Development of the Far East and Trans-Baikal Region to 2025". Adopted by Resolution of the Government of the Russian Federation on December 8, 2009 No. 2094-p, http://gov.khabkrai.ru/invest2.nsf/General_ru/14FDCF99A4F6EEFACA25766B0024C2E5

[26] RIA Novosti, 2012, April 11.

Vladivostok, a city that hosted the APEC Summit in September 2012. The government even adopted a special program – 'Vladivostok City as a Center for International Cooperation in the Asia-Pacific Region'.

In May 2012, the government created the Ministry for the Development of the Russian Far East, setting coordination and implementation of regional development programs and management of the state-owned assets, except for forests and assets in strategic sectors as its prime tasks.[27]

To a great satisfaction of many proponents of rational economic governance, the idea of establishing state-owned corporation tasked with developing Russia's Far East and Siberia has eventually been abandoned. Creation of such a corporation as a subsidiary of the state-run Vnesheconombank (VEB) was among most actively deliberated visions. Opponents, in turn, held that with the mandate as drafted, the corporation may work toward abuse of authority and even more rampant corruption. In November 2011, however, the VEB created a subsidiary – Far East and Baikal Region Development Fund. The new entity pledged to disburse some 70 billion rubles ($2.4 billion) in banking loans by 2015.

In parallel with the government efforts, Viktor Ishaev, the Presidential Plenipotentiary Envoy to the Far Eastern Federal District, has stepped forward with the calls to prioritise regional development projects suggesting to adopt a regional development blueprint until 2050 and invest 3300 billion roubles ($106 billion) in development of the Far East in the next decade.

Indeed, geo-economic realities inform a limited set of options for the economic development of the Far East. Export-oriented model is one that the region has traditionally followed and almost invariably will continue to follow. For that reason, natural resources and infrastructure projects (in particular, transport infrastructure and energy) targeted at the Asian markets have become those attractive areas for private investment.

Only in the past several years, has the officially pursued framework of public-private partnership somewhat materialised, resulting in about 2/3 of the investment incurred by the private sector.[28]

As regards the government-earmarked funding, the evidence is ample that this mode

[27] http://government.ru/eng/power/239/
[28] Interview with Pavel Minakir, director of the Economic Research Institute, Far-Eastern Branch of the Russian Academy of Sciences, http://www.interfax-russia.ru/FarEast/exclusives.asp?id=218714

nurtures various interest groups (governments of different levels, corporations and individuals) schemes, often allowing them to establish control over the regional resource and benefit from their exploitation.[29] The efficiency of government investment is criticised as prohibitively low: some 18 kopecks of return to 1 rouble of investment, while economically feasible investment require a yield of 1.5-2 roubles per 1 rouble of investment.[30]

A set of miscellaneous remarks below serves best to illustrate the scale of the problem:

"The interests of those who undertook to build this pipeline, and the interests of this project have radically diverged. The only concern of those who took to build was to earn as much as possible in any possible way."
(Nikolai Tokarev, the former President of Transneft, on the construction of the ESPO oil pipeline, http://www.rusenergy.com/ru/favorites/)

"I built them, those pipelines, many thousands of kilometres and I can put my head on the block - at any rate, it shall not be more than $ 2 million per kilometre of pipe, unless we talk of the corruption component, of course."
*(*Gennady Schmal, President of the Union of Oil and Gas Producers of Russia, the former deputy minister of construction of oil and gas industry of the USSR, on Gazprom's costs of construction of gas pipelines, http://www.rusenergy.com/ru/favorites/*)*

The Russian Far East does not see as much foreign investment as hoped for. By some estimates, of modest $ 9.9 billion of the total investment, 93 percent was directed to the mining sector and 70 percent was injected in Sakhalin oblast alone. Among the major investors, expectedly, are the companies involved in Sakhalin oil and gas projects. Statistics confirms, of the total amount of accumulated investment the Netherlands hold 48 percent, Japan - 12 percent, the UK – 8 percent, India – 4 and offshore Bahamas and Cyprus - 7 and 5 percent, respectively. Thus, Japan stands out as the second largest investor, while, and, the opposite of expectations, neither China nor South Korea committed remarkable investment in the Russian Far East.

In a region with such particularly high when compared with other Russian territories risks, profit maximisation minded businessmen may consider incurring the risk if and only when a sort of the government backing or guarantee is provided. As presented earlier, the government set a system of region specific regulations aimed to act as incentives for investing in the Russian Far East. Foreign investors may have some assurance of their interests through, for instance, the formats like the PSA or long-term loan-for-oil deals. It is necessary to notice here that both of the examples (practiced in reality) are generally perceived as disadvantageous for Russia.

[29] Tikhookeanskya Rossiya v energeticheckih proektsiyah XXI veka: vektory transformatsii I razvitiya (2012) Russian Center of APEC Studies. April 17, http://www.apec-center.ru/trends/39/168/605/show/
[30] Jurman, Olga (2012) Akademik Minakir:Ideya sozdaniya korporatsii "Dal'nii Vostok" – iz serii neeffektivnogo rukovodstva. April 24, http://www.zrpress.ru/zr/2012/16/52824/

In the above an attempt has been made to show how in fact uneconomical state capitalism's behaviour is in the Far East. If not for the geostrategic reasoning, it is hard to imagine what acts as impetus for the government newly reaffirmed long-term aspirations involving the Far East. It is reasonable to ask now whether, in line with the experts' argument, this inefficiency is spilled out or transmitted in any way externally, to Northeast Asia (NEA).

5. Russia's energy policy in the Northeast Asia[31]

5.1. Geopolitics of Northeast Asia

Speaking of Northeast Asian (NEA) geopolitics, never cloudless the international relations between the states in the region are at times particularly overcast. In 2012, politico-diplomatic ties are especially intensively and repeatedly tested. Also, Japan has been more frequently than any other NEA state involved in open disputes in the region as their immediate side. We briefly exemplify the statement.

On July 3, 2012, Russian Prime Minister Dmitry Medvedev visited Kunashir/ Kunashiri Island, one of the four Kuril Islands claimed by Japan. During this second visit to the Kurils (first took place in November 2010 when Mevedev was president), Medvedev was accompanied by Vice Premier Olga Golodets and Minister for Russian Far East Development Viktor Ishaev. Like the first visit, the latest has resulted in a number of repercussions for the official bilateral relations. Specifically, the official visit by Japanese side, during which bilateral energy cooperation agenda was planned to be discussed among other matters, has been postponed. In the past several years, Japan is overtly concerned over the possibility of China's participation in joint with Russia economic development of the islands. Such a scenario was contemplated by Russian Minister of Foreign Affairs Sergey Lavrov and was fiercely objected by the Japanese MoFA.[32]

On August 10, 2012, the then President of South Korea Lee Myung Bak visited Takeshima/ Dokdo Island which is claimed by Japan. In response to this move, then Japanese Prime Minister Yoshihiko Noda sent a personal letter deploring the president's visit to the disputed island, which South Korean side refused to receive. Japanese MoFA, in turn, refused to allow a South Korean Embassy official to enter the ministry to return Noda's letter. Japan is said to be planning to lodge a suit with the International Court of Justice. The incident has complicated the bilateral economic ties, including the bilateral currency swap expansion deal and Japan's planned purchase of South Korean government bonds.

With China, Japan experienced a new round of escalation in a territorial issue over the Senkaku/ Diaoyu Islands. On August 15, 2012, the Hong Kong activists landed on one of the disputed islands. This act may be seen as one of the developments following the

[31] In the present study, Russia's energy relations are analysed with three Northeast Asian states: China, Japan and Korea (NEAs or NEA-3).
[32] RIA Novosti, February 11, 2011, http://ria.ru/economy/20110211/333236516.html

Tokyo Metropolitan Government initiative voiced by Governor Shintaro Ishihara in April 2012 during his visit to the USA. The Tokyo Government's plan to buy three of five privately owned islands was taken over by the national government which finalised the deal in September 2012. The step caused an unprecedented upsurge of anti-Japanese sentiments in China. The bilateral diplomatic relations have reached an impasse on the eve of their 40-year anniversary. Japan-China relations were also seriously impacted in September 2010, when a Chinese fishing boat collided with the Japan Coast Guard ships.

Another flash point in the NEA is the Democratic Peoples' Republic of Korea (DPRK) whose proliferation agenda is by far exceeding the scope of the regional security. In addition to a number of historical controversies between the DPRK and Japan and South Korea, there have been recent disruptions of military and political tensions. In 2010, South Korean naval ship Cheonan sank and 46 of its sailors died in an incident blamed on the DPRK. Also in 2010, the DPRK shelled South Korean Yeonpyeong Island, killing two marines and two civilians. Several times in 2009 Japan was alerted by the missile tests conducted by the DPRK to the Sea of Japan. Japan reasonably questioned the real intentions and targets of the tests conducted by the DPRK regime.

These developments illustrate that geopolitical environment of NEA remains unstable. While Japan seems to be challenged by its most influential neighbours in the region, the country's alliance with the U.S. is also believed to be not in its best shape. These external complexities are coupled with a number of domestic economic and political challenges, to an extent aggravated further by the triple disaster which hit Japan in 2011.

Geopolitical environment certainly complicates geo-economic situation in NEA. Take energy, the world's largest importer of LNG and the third largest oil importer Japan faces increasing competition from South Korea for almost identical sources of oil and gas. In turn, bordering the DPRK South Korea is unable to utilise the benefits of energy export via pipelines and left with limited options for more expensive and risk-averse energy imports. In this context, although much more geographically diversified, China's energy import, nonetheless, additionally tightens the Asian markets due to the country's large and continuing to grow demand and drives up the prices.

The result of geopolitical environment is geo-economic irrationality. Large and influential economies with a certain degree of complementarity have no established mechanisms for intra-regional cooperation.

5.2. Russia's energy governance and Northeast Asia

Russia's relations with the Northeast Asia countries have seen ups and downs and have developed at different tempos. A 'triple shocks' framework seems to be helpful in identifying the main currents that have steered Russia towards the NEA. "*The 'triple shocks' – the end of the Cold War, the 1997 Asian financial crisis,*[33] *and the 9/11 terrorist attacks – each played a role in pushing forward … Russian evolution from neofeudal governance*[34] *and a strategy of disengagement to neoabsolutist governance and a more neomercantilist strategy*".[35]

In the early 2000s, two competing visions were formed of the future development of Russia's oil and gas sector in relation to Northeast Asia. One was planned by private companies (Yukos, Lukoil, TNK and Sibneft), and was 'ideologically' inspired by Mikhail Khodorkovsky. Had this grand plan been implemented, the geography (and geopolitics) of Russia's energy relations would have been significantly entrenched along two arches – one Chinese (with the Angarsk – Daqing oil pipeline as the pivot) and one American (the Western Siberia – Murmansk oil pipeline) with a major role played in the sector by private business. However, it was decided to develop Russian energy with the government's active involvement. The narrative is well-known: in 2004, the state rather swiftly redrew the plan revolving around Yukos' vision, but did not embark on its implementation as hurriedly. It took several years for a principle decision to be made concerning a spatial format for Russia's involvement with the countries of Northeast Asia – 'the China card', 'China and beyond' or Northeast Asia. During this lingering vagueness, the NEA states were attempting to suggest to Russia their visions of possible formats and offer various means to enhance energy cooperation. While Russia vacillated, the NEA states entered a 'scramble for Russian energy'.

It is now admitted that it was Japan that[36] managed to convince the Russian government not to play the 'Chinese card' only, but to make a decision opening up prospects for engaging with the broader Asia Pacific Rim.[37] This Japan did through its

[33] Albeit further in his work the author speaks entirely about aftermath of the Russian 1998 financial crisis, which makes more sense in the given theme.
[34] This refers to a federal system which emerged after the demise of the USSR with its centre - periphery relations.
[35] Northeast Asia. Ripe for integration? (2008)/ Ed. by Vinol K.Aggarwal, Min Gyo Koo, Seungjoo Lee, Chung-in Moon. Berlin: Spinger-Verlag. p.180.
[36] East Siberia (federal subjects of the *Siberian Federal District:* Krasnoyarsk Krai, Irkutsk Oblast, Buryat Republic and Zabaikalsky Krai), and the Far East (federal subjects of the *Far Eastern Federal District*: Amur Oblast, Jewish Autonomous Oblast, Kamchatka Krai, Magadan Oblast, Primorsky Krai, Sakha Republic, Sakhalin Oblast, Khabarovsk Krai, Chukotka Autonomous Okrug).
[37] For more detail see: Shadrina, Elena (2004) Energy cooperation in Northeast Asia. JIIA Fellowship Occasional Paper 27.- Tokyo: The Japan Institute of International Affairs

promises to allocate sizable amounts of investment in energy, transport and social infrastructure in East Siberia and the Far East. Apparently, shifts in Japan's and later in Korea's energy import policies envisaging the involvement of Russian resources contributed to Russia's decision to set about developing the resource base in the Russian East.

Once the decision was made and it became clear that the Russian government was set to play a key role in developing the oil and gas sectors in eastern Russia, the NEAs started demonstrating their interest. This aspect – the possibility for government-to-government agreements as a means to guarantee the energy security of both sides involved – played a positive role in the NEA states' aspirations to embark on more extensive participation in energy projects in eastern Russia. The number of NEA-based NOCs and smaller business units entering oil and gas segments in the Russian east has increased significantly.

The role of inter-governmental contacts within the Northeast Asian context is worth emphasising. Bilateral ties involve various actors, but in NEA companies do not usually engage themselves in risky activities unless governmental agreements have been struck. To some degree, this is because the government in this situation is regarded as the most credible actor and guarantor (despite all the great variation in the economic systems of the NEA states). Also, Northeast Asia's regionalism (primarily framed by functionalist thinking) remains very weak and this contributes to the overall environment for cooperation, which is significantly different from what is observed in Europe, or North America, or even in South-East Asia. Largely due to these attributes of the region, Russia's policy-making rather fairly complies with the NEA states' norms and even acts as a catalyst enhancing energy cooperation on this flank.

Addressing the issue of the viability of the government-to-government format for Russia's cooperation with the NEA troika, some comparative lines between the NEA states' national energy policies may be drawn. There are certain commonalities which derive from similar concerns about a deep dependency on energy import. Such include high concentration of imports from a limited number of suppliers (dependency on the Middle East as a major threat), high volatility of energy markets, deteriorating environment and so forth. As a whole, these factors justify the government's more

<http://www2.jiia.or.jp/pdf/russia_centre/h15_cis/12.pdf>, and Shadrina, Elena (2004) Is Pacific oil pipeline to breathe new life into Far Eastern economy?/ In 平成１５年度 外務省委託研究報告書. ロシアＣＩＳの資源戦略調査。平成１６年３月。財団法人日本国際問題研究(Report on the year 2004 study on Russia and CIS countries` Resource Strategy. Ministry of Foreign Affairs: Japan Institute of International Affairs. March 2005).

active involvement, which can be best seen through the SOEs' presence.

5.3. Russia's energy relations with Northeast Asian countries

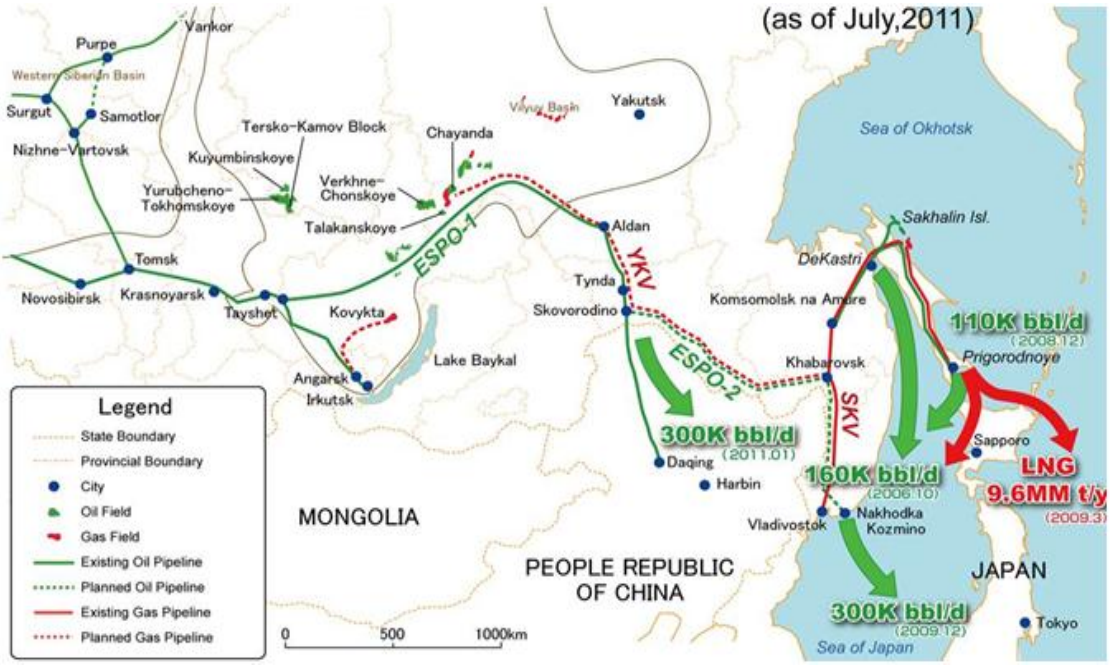
"Gazprom's talks with China remind me of an old anecdote: Market. All trade in apples for 20 RB/ kg, but one man offers the very same apples for 100 RB/kg. When asked "Why?", he replies, "Money are desperately needed."

*(*Mikhail Korchyomkin, Director General of East European Gas Analysis, on prospects for the Russo-Chinese agreement on gas, http://www.rusenergy.com/ru/favorites/*)*

Policy emphasis on the expansion of energy cooperation with Asian countries, called 'the Asian vector', was proclaimed in 2003 in the Energy Strategy until 2020. It was initiated to reduce Russia`s over-dependence on the European market, minimise risks associated with transit, and, not least, enhance the economic development of Russia's eastern regions. To meet these ambitious goals in the East, the government has established, as was outlined in the preceding sections, a range of sector- and region-specific initiatives.

The remarkable developments in Russia-NEA oil and gas relations (Map 1) over the past several years need to be recognised as a general result.

Map 1. Russia's Northeast Asia-oriented oil and gas projects



Source: JOGMEC.

The progress is largely the outcome of much earlier agreed and recently accomplished projects, but also a result of a broader geopolitical environment impacting energy

markets. Russia increases the volumes of oil and gas exports to NEA, gradually eroding the dominance of the Middle East and replacing Iran.[38] The latter was rather significant supplier of oil to the NEA countries, providing about 10 percent of Japan's and South Korea's oil imports and over 11 percent of China's oil imports, as of 2011. Amidst the sanctions against Iran, Japan and Korea at some point briefly banned their imports from Iran, but resumed the trade although in a smaller scale and under a new arrangement for marine insurance. In the situation when the European insurers stopped their transactions for Iran, the Japanese and Korean governments now provide a guarantee on insurance for the national shippers of the Iranian oil, the Chinese government, however, opted for letting the Iranian side insure its marine supplies. More independent in foreign policy China does not consider any reduction and, quite the opposite, increases its purchases of the Iranian crudes.

Comparable with Iran in terms of supply volumes, Russia is somewhat substituting the elapsing imports. Looking from this perspective, Russian oil supplies to NEA will almost certainly grow. Additionally, a new player in the LNG market, Russia covers about 4 percent of Chinese LNG imports, about 10 percent of Japan's LNG imports[39] and some 8 percent of Korea's LNG imports,[40] as of 2011. Russia's prospects in the entire Northeast Asian LNG market are rather solid. Additionally, the post-Fukushima nuclear-power sensitive Japan is expected to increase its oil and LNG imports from Russia more significantly than other consumers in the region.[41] Currently, Russia's dependency on NEA-3 markets can be characterised as low for oil and high for the LNG. That is, in 2010, of the total volumes of Russian oil exports 3.9, 4.3 and 5.5 percent were shipped to Japan, Korea and China, respectively. As regards Russia's LNG exports, 62, 29 and 4 percent were sent to Japan, Korea and China, accordingly.[42]

The NEA countries (especially Japan and Korea, but also, and increasingly so, China) are distinguished by their profound dependence on energy imports and especially high vulnerability against the Middle Eastern supplies (Shadrina 2010b, 29). Major consumers, in the future the NEAs are expected to diverse in terms of their demand. China's profile is of particular prominence. The country's future demand for the imported fossil fuels will however not grow as fast. China adopted a national plan to

[38] Schmollinger, Christian (2010) Russian Oil Erodes Middle East's Hold on Exports to Asia: Energy Markets, *Christian Science Monitor*, July 8.
[39] Daily Yomiuri Online. January 28, 2012.
[40] Asia Energy Links, https://eng.rim-intelligence.co.jp/news/select/category/overseas/article/84465
[41] http://interfaxenergy.com/natural-gas-news-analysis/asia-pacific/japans-lng-imports-spike-in-january-2012/
[42] Russian APEC Study Center, http://www.apec-center.ru/trends/39/168/604/print/

2030, envisioning the transition to a low carbon economy. Additionally, China stands to increasingly utilise nuclear energy, building for that end 27 (the largest number) new nuclear reactors. Similarly, Korea endorsed a plan to 2030 envisaging an increase in renewable and alternative energy, but also targeting at a higher proportion of nuclear energy (10 new nuclear reactors are under construction). In Japan, the re-opening of oil, gas- and coal-fired plants implemented immediately after the Fukushima resulted in swollen fuel imports. Since, according to the recently adopted New Basic Energy Strategy, Japan intends to be free of nuclear energy by 2030, demand for fossils will increase, although the extent of such an increase depends on the progress with renewable energy (which is given priority).

Although from 2009-2010 there was a remarkable dynamism in Russia's cooperation with NEA (the Sakhalin II LNG plant and the ESPO-I were launched), Russia has competitors here. In relation to China, especially strong positions against Russia have the Central Asian states due to their abilities to supply gas via the newly built Turkmenistan-Uzbekistan-Kazakhstan-China pipeline. In relation to Japan (and potentially Korea, too), Russia's new competitor is now transforming from latent into a real rival. The USA's shale gas revolution has become a reality for the Asian markets, too. In 2012, a number of Japanese utilities concluded the long-term contracts with the North American exporters and the Japanese government has stated its intention to increase the share of North American LNG to 20 percent of the current level of LNG import.[43] Apparently, Russia needs to seriously consider its further strategy in such an attractive market. Until now, Russia evaluated its position here as rather strong with additional arguments being anticipated reduction in LNG exports of Indonesia and Malaysia,[44] the two are traditional suppliers of LNG to NEA.

The Russian Ministry of Energy operates by estimate that by 2020 Russia may count on China's demand for Russian gas of 60 billion cm/ year. By some estimates, 25 percent of Russia's total gas and 15 percent of its total oil resources are located in East Siberia and the Far East. However, data on Russia's hydrocarbons located eastwards are inexact, as only 6 percent of the continental shelf and 7.3 percent of the onshore area have been covered by geological exploration.

Gazprom estimates gas reserves at 52,400 bcm on-shore and 14,900 bcm off-shore, part of which could benefit the Northeast Asian states. In the vast area of East Siberia

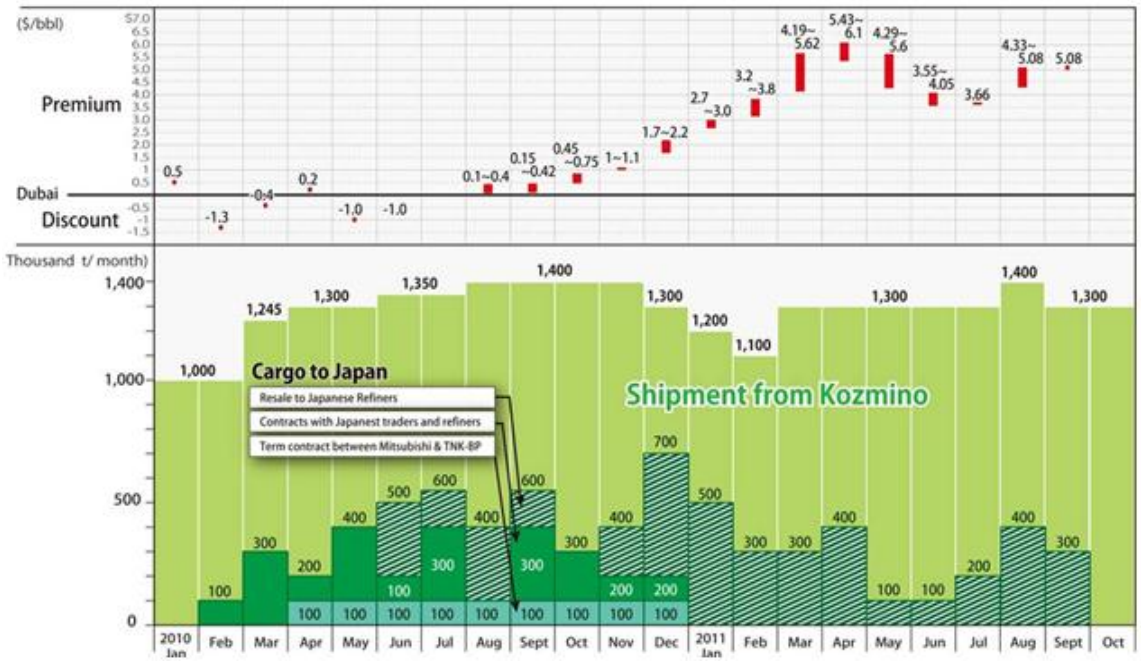
[43] Platts. July 3, 2012, http://www.platts.com/RSSFeedDetailedNews/RSSFeed/NaturalGas/7815031
[44] A result of two-fold challenge: depletion of domestic gas reserves and growth in domestic energy demand.

and the Far East, Gazprom is pursuing an ambitious Eastern Gas Programme, which envisages gas output at over 200 bcm annually by 2030 (from 8 bcm in 2006). Four centres (Krasnoyarsk, Irkutsk, Yakutia and Sakhalin) of gas production in East Siberia and the Far East are scheduled to be activated depending on the degree of their current development. Initially domestically-oriented, the Sakhalin-Khabarovsk-Vladivostok and Yakutia-Khabarovsk-Vladivostok gas pipelines have recently been planned to become a part of the transport network enabling future exports to China and Korea.

Gazprom has long hoped to open up a supply relationship with China (this is believed to be one of the reasons behind Gazprom's interest in Sakhalin I), but no fruit has yet been yielded. Russia and China signed a memorandum of understanding (MoU) in March 2006, agreeing on up to 80 bcm of annual exports to China from 2011. A similar agreement was signed with Korea in October 2006. In principle, two export routes have been considered: the western one (the Altai project relying on the Siberian fields and directed to China) and the eastern one (gas of Sakhalin origin transported through the system of domestic pipelines for both internal consumption and export to China and Korea). Due to apparent disagreement with China on price (Gazprom has pushed for netback parity with its sales to Europe, but China refused this as unacceptably high), little progress has been achieved in subsequent years. Thus, the prospects for piped gas exports to the NEA remain blurred.

Russia's prospects in NEA oil market seem promising. Mainly owing to China's oil demand, the Asian market is large and vibrant. Also, the infrastructure enabling Russian oil export to the Asia is gradually coming in place, thereby solidifying Russia's energy ties with the NEAs and transforming these relations into a long-term format. For Russia, closer involvement with the Asian market is a plus because in this market Russian new oil blend ESPO yields a higher (compared to Russian traditional blend Ural) price (Graph 6). For their part, the NEA economies, traditionally experiencing the Asian premium, are willing to increase new Russian oil flows. Adding to the economic benefits, the time required to deliver Russian exports to the Asian markets is significantly shorter – just five days - while the delivery of supplies from the Middle East, Africa and Brazil requires at least two-week's sailing. Also, considerations of the security of sea lanes (especially the Strait of Hormuz and the Strait of Malacca) favour Northeast Asian oil imports' switch towards Russia's greater share in it.

Graph 6. Oil shipments from port of Kozmino and price dynamics of the ESPO blend



Source: JOGMEC.

Taking up the issue of efficiency or, rather, inefficiency of the Russian government energy policy in the east of Russia, while the ESPO price seems to be indeed a solid prove that some of the calculations were correct, there are, nevertheless, facts showing the opposite. Strictly speaking, the ESPO's commercially viability is questionable. Seeking to facilitate the eastwards shift in Russian oil export, the Russian government decided to subsidise ESPO-borne exports by suspending export duties on East Siberian oil (to be partially re-enacted from July 2010) and through a preferential transport tariff for the ESPO crude (set at $50/t, while the actual cost is $130/t). The Ministry of Finance was strongly opposing any further extension of these 'eastern tax holidays', pointing out the budget losses of some 120 billion roubles in 2010 alone.

Additionally, Russia has experienced some complications over the ESPO exports to China. To be concrete, in January 2011 CNPC started paying a smaller amount than provided for in the 20-year contract. The issue under dispute was the cost of transporting crude through Russian territory via the ESPO pipeline, which according to the Chinese has been overestimated by approximately $30/ t. While the Russian side argued that the price of transporting oil should be calculated based on the entire route of the ESPO pipeline to the end point of the port terminal in Kozmino, China insisted

that the price formula should only include the cost of transportation from Skovorodino, which is 2,046 km from Kozmino. It is unclear how this misunderstanding was overlooked at the beginning when China provided Transneft and Rosneft with loans of $10 billion and $15 billion, respectively, for guarantees of long-term oil deliveries of 6 million tonnes and 9 million tonnes, correspondingly. In the debate, Transneft went as far as expressing its intention to pay out the loan ahead of the agreed schedule. After many rounds of talks, the issue has been settled, but in July 2011, for instance, the Chinese cut their oil import by half indicating their displeasure over the pricing mechanism. Unfortunately, the possibility for the scenario to repeat cannot be played down.

Having stepped up the Asian course, Russia has plans for the further development. The future of Russia's energy cooperation with NEAs can be presented as involving the following major projects (Table 1).

Table 1. Russia's Northeast Asia-oriented projects

Operational	Projects	Oil	LNG/ Gas
	Sakhalin I, II	*	*
	ESPO – 1	*	
Under development/ projected	ESPO – 2 Sakhalin III Eastern Route (Sakhalin – Khabarovsk – Vladivostok & Irkutsk - Yakutia – Khabarovsk – Vladivostok) Altai gas pipeline (Western Route) LNG plant in Vladivostok	* *	* * *

Source: composed by the author.

These projects are at different stages of their life cycles and the development progresses at different speed. The most problematic and long-standing on cooperation agenda is gas pipeline, which due to the reason of space is not discussed here.[45]

Adding one more note on competition, notorious for its denial of the evident progress of shale gas, Gazprom has now clearly realised a fallacy of such an approach. That is why the recently released IEA report about the U.S. as a shale oil producer and the

[45] For more detail see: Shadrina 2012c.

country's promising profile to take over the Saudi Arabia and turn into net-exporter by 2035 [46] was received by the Russian government with much more thorough consideration. [47] Increasingly driven by technological revolutions and technical evolutions, contemporary energy affairs make it absolutely crucial for the companies especially of Gazprom's profile and the nations of Russia's specialisation to be farsighted, flexible and innovation-intensive. Given that the Far East is the land of greenfields, there is, in fact, that very chance for Russia to start here a new more efficient and technologically advanced mode of the energy resource development.

Despite the overall environment for the international cooperation in NEA remains strained by complex nodes of the territorial disputes and proliferation issues, Russia's energy linkages with the countries in the region are becoming stronger.

Japan can be rightfully credited as Russia's traditional and one of its most loyal partners. Japan contributed the most among the NEAs to the development of the Far Eastern energy projects in the past and demonstrates its interest in further expansion of energy cooperation. With China, Russia has the most diversified energy contacts, including those on nuclear facilities construction, petrochemical products production and hydro power electricity generation. Nonetheless, the bilateral energy dialogue is often formatted in the way which seems to be more beneficial to China. One case exemplifying the said is the price for Russian energy resources. China has in fact managed to gather more negotiating power over Russia owing in particular to its deeper involvement with the Central Asian states, but also owing to China's stronger financial capabilities, which have been extended to Russian Rosneft and Transneft in the form of loans. Perhaps the larger format of the deliberated Shanghai Cooperation Organisation Energy Community may to a degree help Russia level off its status against China. Finally, Korea, which compared to China and Japan initially appeared relatively less interested in energy cooperation with Russia, has come to form oil and gas ties with Russia and is now a very influential negotiator in the matters of construction of the gas pipelines.

Rather differing features of Russia's energy ties with each of the Northeast Asian states can be combined under a broadly defined pattern in which inter-governmental dialogue determines the overall discourse. That is why the spatial image of energy cooperation in Northeast Asia can best be presented in a hub (Russia) and spoke (the rest of the countries in the region) perspective. There are yet only a few multilateral forums of a

[46] http://www.hydrocarbonprocessing.com/Article/3116673/Latest-News/Shale-boom-to-enable-US-to-overtake-Saudi-Arabia-as-top-oil-producerIEA.html
[47] RusEnergy, November 30, 2012, http://www.rusenergy.com/ru/news/news.php?id=63528

mainly ad hoc nature that inform the framework for the energy cooperation between Russia and the NEAs.

6. Summarising thoughts and policy implications

State capitalism, as studies evidence (Dupuy and Truchil 1979; Aligica and Tarko 2012), does not require a new theory depicting it as a new economic system. Because it does not reveal a true novelty in terms of basic structural elements of economic system organisation, state capitalism "*must be used as an analytical category*" (Dupuy and Truchil 1979, 32). Aligica and Tarko claim that more justified approach to state capitalism would be to perceive it as the implication of rent-seeking behaviour. Studies on state capitalism largely converge on identifying its built-in inefficiencies and emphasise the latter's negative impact on other globalised economies. While some of the studies claim that it is for this very reason of ineffectiveness that state capitalism is not to see such a long life (Bremmer 2009a, 2009b, 2010, 2011; The Economist 2012), others utilise a comparative prism stressing that inefficiencies are relative, not absolute, and a survival or may well be even a triumph of state capitalism is a matter of vigour and competitiveness of the market economies themselves (Aligica and Tarko 2012). While this remains to be seen, the fact is that the states have activated their roles in economic governance and the overall perception about the borders of the state's economic intervention has become less categorical (Helm 2010).

That being said, a work discussing state capitalism as a socioeconomic phenomenon almost unmistakably covers the following dimensions:

- the strength of the state both domestically and externally;
- the character and extent of the state's interventions in national economy; and
- the nature and intensity of the ties between the government and interest groups[48].

Three elements can be clearly identified here: the actors who govern, the actors who are being governed and the means through which the process of governance takes place. In principle, the phenomena at hand – state capitalism – is the one from the realm of governance.[49] The World Bank defines governance as "*… the manner in which management power is exercised in the country's economic and social resources for development*"[50] and "*… the traditions and institutions by which authority in a*

[48] On interest group see: Weber, Max (1962) *Basic Concepts in Sociology.* The Citadel Press.
[49] On governance see: Shadrina, Elena (2012) Government and Governance: Traditional and Novel Research Agenda, *http://www.kisc.meiji.ac.jp/~follow/topics/AP/ElenaShadrina.pdf*
[50] Managing development - The governance dimension (1991). The World Bank Discussion Paper No. 34899. Washington D.C. p. 1, http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2006/03/07/000090341_20060307104630/Rendered/PDF/34899.pdf

country is exercised…"[51] In this light, it is tempting to propose considering a treatment of state capitalism as one of the forms of governance.

An expedient framework for the analysis of Russia's state capitalism, as believed, needs to be built upon two pillars: spatial dimension and natural resource endowment, both the important notions from the realm of economic geography.

Ongoing energy policy transformation in Russia reflects an eventual arrival of Eurasianism (Shadrina 2010ab) in Russia's policy making. Considerations of pragmatism of domestic and external origin define Russia's state capitalism. At times when Russia's practices are increasingly incompatible with Western values (such as free competition, the rule of law, the transparency of decision-making processes and so forth), more flexibility and cooperativeness can be attained through the partnerships in the East.

Asianisation as a policy course is deeply pragmatic (Shadrina 2010ab, 2012c). There are objective factors increasing the attractiveness of the NEA market, such as an already significant level of energy demand, which is projected to grow (whereas the trend in the EU is stable or even declining). The geographical proximity of the NEA states is also particularly favourable, granting Russia the direct access to NEA consumer markets without any transit or intermediary issues involved. Furthermore, the resource base adds to the attractiveness of the Asian markets: in the Russian east, the resource base is largely untouched (unlike in the intensively exploited and greatly depleted provinces of Western Siberia), but believed to contain huge reserves. The logic of advancing the socio-economic development of Russia's eastern regions through the synergic effect of enlarged, international energy cooperation with the NEA countries is also incorporated in the policy-making process.[52]

Energy policy-making involves a permanent trade-off, where economic and geopolitical reasoning interplay. In the past, Russia has frequently been accused of its politically motivated decisions on the matters of energy relations with the EU. On the eastern flank, in NEA, in particular, security considerations predominate over commercial thinking (Shadrina 2010b). Russia's overall energy policy should be perceived as a function of a variety of parameters, such as the country's industrial structure, resource allocation, spatial dimension, geopolitical location, etc.

[51] A decade of measuring the quality of governance (2006) The World Bank. Washington D.C. p. 2, http://siteresources.worldbank.org/INTWBIGOVANTCOR/Resources/1740479-1150402582357/2661829-1158008871017/booklet_decade_of_measuring_governance.pdf

[52] The importance of this aspect is specifically underlined in the Programme for Effective Exploitation on a Systemic Basis of Foreign Policy Factors for the Purposes of the Long-Term Development of the Russian Federation, February 2010.

Russia's state capitalism, especially in oil and gas sectors, is nourished by external factors. Two aspects need to be addressed here. First is economic efficiency. Russia's state capitalism in energy sector is shaped by the government's attempts to improve economic performance in the industry. The known fact is that the energy exports generate much larger profits as compared to sales on the domestic market due to the price difference. An example to the point, Gazprom's 40 percent sales in external markets generate 70 percent of the company's revenues. From this perspective, Russia's move eastward is absolutely rational. When European markets gradually become less lucrative for the Russian suppliers (a result of European competition policy and successful energy exports' diversification), new export markets are essential. Given the level of NEAs' current demands and the prospects for their further growth, NEA is one of the most attractive markets.

The latter is mainly generated by China, who is a net-importer of oil from 1993 and a net-importer of gas from 2007. According to the BP Energy Outlook 2030,[53] China's oil consumption forecast to reach 17.5 million barrels/day by 2030, overtaking the US to become the world's largest oil consumer. China's dependency on imported oil, according to the IEA,[54] will increase from 54 percent in 2010 to 84 percent in 2035. As regards the gas, the overall role of gas in China's energy mix is small – about 4 percent (with the projections to reach 10 percent by 2020)[55], but the scale of demand and the rate at which it grows make China a very attractive customer to the gas exporting countries. According to the IEA's WEO 2011, China's gas demand is predicted to increase by 5.4 times to 502 bcm in 2035. BP Statistics forecasts gas consumption in China to grow at 7.6 percent annually to a level of over 1.2 bcm/day in 2030. Domestic gas production is expected to grow 6 percent per year. Despite non-conventional gas is expected to contribute some 41 percent to this growth, there will be nonetheless a rising need for imports. The IEA projects that China's dependency of natural gas imports will increase from 9 percent in 2009 to 41 percent in 2035.

Japan's post-Fukushima energy policy also spells in more opportunities for Russian energy exporters. According to the BP Statistical Review of World Energy,[56] After

[53] BP Energy Outlook 2030. London. January 2012, http://www.bp.com/liveassets/bp_internet/globalbp/globalbp_uk_english/reports_and_publications/statistical_energy_review_2011/STAGING/local_assets/pdf/2030_energy_outlook_booklet.pdf
[54] World Energy Outlook 2011. Paris: International Energy Agency, 2011 (WEO 2011).
[55] Cutler, Robert M. (2011) China's Gas Imports Jump. *Asia Times Online*, June 24, 2011, http://atimes.com/atimes/China_Business/MF24Cb01.html
[56] BP, 2012. Statistical Review of World Energy, http://www.bp.com/assets/bp_internet/globalbp/globalbp_uk_english/reports_and_publications/statistical_energy_review_2011/STAGING/local_assets/pdf/statistical_review_of_world_energy_full_report_2012.pdf

Japan's nuclear output fell by 44.3 percent in 2011, the need in alternative sources for electricity generation grew resulting in larger imports. In 2011 Japan's gas consumption augmented by 11.6 percent and the LNG imports increased by 12.5 percent, while consumption of fuel oil augmented by 29.7 percent.

Second consideration lies in the area of geopolitics. Russia's official relations with the states in NEA, with the only exception being Japan, seem to be of no particular problem. Although the discussion of China's growing assertiveness and outgoing ambitions is taking place in Russian academia and think tanks and the developments are watched out carefully by Russia, in the eyes of the rest of the world, the two states exhibit unending consensus on the matters of global politics even when regards the questions as sensitive as Iran's and the DPRK's proliferation, war in Syria, and earlier, war in Libya. Russia soberly evaluates its role in economic ties with China (a role of resource appendage, as Russian analysts traditionally put it), attempts to manoeuvre for a better pattern but objectively has a limited set of tools in doing so. Stumbled for years Russia-China gas negotiations is one of the most notorious cases.

Interestingly, in April 2012, Renmin Ribao has published the results of the poll about Russia's major problems which not only impede its own economic progress, but slow down the bilateral relations. The list includes six most serious problems, among which there are: depopulation and shortage of skilled labour, underdevelopment of financial sector and business' low ability for self-organisation, high dependency on raw materials export and shrinking share of technological and processed goods in export, increasing barriers for investment and economic activity, widening technological, innovative and entrepreneurial gap, monopolies' dominance and lack of competition.[57] Agreeing with China's criticism, Russian pundits point out that Putin's list of five priority tasks for Russia's development made public on April 11, 2012 has one converging with the Chinese version point – the need to address the problem of depopulation. The other imperatives emphasised by Putin included a pressing need to develop East Siberia and the Far East, develop new (innovations and knowledge intensive) economy, create quality jobs and implement foreign policy fully activating Russia's Eurasian status.[58]

Geopolitics indeed greatly influences economic ties in NEA. Japan-China territorial bust-up in September 2012, for instance, spawned rampant anti-Japanese sentiment in China with numerous acts of vandalism and rioting at the Japanese-owned businesses.

[57] Bashkatova, Anastasiya (2012) Pekin Postavil Putina v Bezvyhodnoe Polojenie (Beijing Has Put Putin in a Despaired Position). *Nezavisimaya Gazeta*. April 17.
[58] Vladimir Putin, Report to the State Duma. April 11, 2012, http://premier.gov.ru/events/news/18671/print/

China-linked Japanese businesses reported losses of trillions of yen and yet uncertain whether or to what extent they can resume their operations.[59] This illustrates the scale of political risks of keeping the bilateral disputes unsettled. Taken regional risks juxtaposed with Russia's traditionally high country risk, it is not surprising that a kind of guarantee from the Russian government is a precondition for a foreign investor to step in an energy project in the RFE. In other words, geopolitical risks require the state's involvement and, in fact, so far no energy project has been implemented in the RFE without a bilateral intergovernmental framework established first.

To commence energy cooperation with NEA states and ensure the development of this, the Russian government has offered unprecedented fiscal and other incentives. As the institutionalisation of the multilateral cooperation in the Northeast Asian region is rather weak, the policy framework is chiefly informed by bilateral intergovernmental agreements and energy dialogue formats. Importantly, provisions on a 'regional component' envisaging the enhanced economic development of East Siberia and the Russian Far East are the key elements of both agreement and dialogue formats.

Finally on the account of state capitalism and compatibility, it appears that state capitalism is not an alien practice in the NEAs themselves. There is obvious if not similarity, then certain degree of structural cohesiveness between the energy industries in the countries. Like in Russia, the state's hand is pronounced in NEAs. In Korea, for instance, established by the government in 1983 Korea Gas Corporation, Kogas, enjoys almost entire monopoly in the gas industry and stands out as the world's largest LNG importer. Another major - Korea National Oil Corporation - controls the extraction of hydrocarbon resources. In Japan, Japan Oil, Gas and Metal Corporation, JOGMEC, is a Japanese government Independent Administrative Institution. Created in 2004 as the result of merge between the former Japan National Oil Corporation and the former Metal Mining Agency of Japan, JOGMEC is tasked with securing stable supply of natural resources. In 1998, China reorganised domestic energy industry in order to separate regulatory and administrative functions. The state-owned China National Petroleum Corporation (CNPC) is the largest company of China. In 1999, as part of restructuring, CNPC created PetroChina transferring most of its assets in exploration, production, refining, marketing, chemicals and natural gas businesses. CNPC and PetroChina develop overseas assets through a joint venture, CNPC Exploration and Development Company, which is 50 percent owned by PetroChina. In 2010, PetroChina became the world's second largest company in terms of market

[59] The Japan Times. October 7, 2012, http://www.japantimes.co.jp/text/nn20121007a8.html

capitalisation. State-owned China Petroleum and Chemicals Corporation (or Sinopec group) is China's second largest (after CNPC) and Asia's largest oil refining and petrochemical company. Shinopec competes with China National Offshore Oil Corporation (CNOOC Group), which focuses on the exploitation, explorations and development of oil and gas offshore China.

Having abandoned the eastern regions accounting for 1/3 of the Russia territory for over two decades since the beginning of the market transformation, the Russian government has eventually faced with the grave consequences of the region's shrinking populace, decaying industrial base, unemployment, decreasing living standards, etc. The government seems to have ultimately re-found a suitable framework for the regional policy here. In the situation of major developmental projects' rather weak feasibility or their altogether economic unsoundness, a policy pattern based upon the state's strong role with a limited room for the private initiatives seems to be but only available policy mode. Russia's cooperation with Northeast Asia and Russia's energy policy tailored to enable such a cooperation need to be understood as a pragmatic choice made by the Russian government in order to address multifarious domestic concerns.

Turning to policy implications, Russian state capitalism should be understood as a mode of governance which serves the purpose of establishing and maintaining the government's control over the resource rents for the sake of safeguarding the existing system and buffering it from socio-economic and political changes, which, if profound enough, may endanger the government's very existence.

External factors informing the environment for energy policy are different in west and east to Russia. While the EU's energy policy gradually becomes more consolidated and its energy demand for Russian carbons is flattening resultant of both Europe's energy imports geographical and structural diversification and the overall economic difficulties persistent in the euro-zone, Russia eventually faces a shrinking room for manoeuvre and experiences a declining influence on the European consumers. NEA countries, to the contrary, have no unified stance on energy cooperation with Russia, divided by territorial disputes and distrust neither they seek to establish such. In this geopolitical context, the Russian government commences grand energy projects oriented at Asian markets.

Economics of energy projects in the Russian Far East is significantly worse when compared with that in traditional energy producing territories. To an extent, the former is hoped to be compensated by a higher than in any other market price level (due to

the Asian premium). The main bill-payer is, however, the Russian government, which heavily involves itself in the far-eastern energy resource development, launching to this end a vast system of subsidies. To legitimatise domestically a policy of yet rather dubious efficiency, the government needs to wrap it in a context of a larger developmental project for the entire region.

The Russian Far East has already become that chain that links Russia with the NEA countries, but it is highly likely that energy policy at such a cost would be the Russian government's last enterprise. There simply may be no sufficient financial means to be thrown at the development which is unlikely to result in commercially satisfactory returns. It is equally unclear if Russia stands to reap any substantial geopolitical benefits in NEA. While energy demand of NEAs grows, so does economic power and geopolitical grip of some of the NEAs' states. Here, the first case to think of is certainly China.

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