

Commemorative Paper

Northeast Asia: Past and Future

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A New Locomotive of Growth

In the late 1980s Robert Scalapino¹ put forward the concept of "natural economic territory", having in mind the objective of predisposing Northeast Asia toward the development of economic cooperation between its constituent countries. This was based on the natural distribution of factors of production and economic resources in this subregion of the Asia-Pacific. The presence of two groups of countries with complementary economic resources is the basis of this concept. Subsequently the concept was further developed by many researchers from the countries that are part of this subregion as: a "regional Sea of Japan" concept; a "Sea of Japan Rim" concept; and an "integration of the economies of Northeast Asia" concept.²

Generally, this idea—economic cooperation within the framework of Northeast Asia—was received in Russia, as well as in other countries of this subregion, with enthusiasm. Theoretically this enthusiasm was based on its familiarity—this idea correlated very well with the theory of zoning and productive forces allocation, a territorial division of labor that was conditioned by resource complementarity.³ This concept also suggested a very simple interpretation of the economic advantages of the partners in this integration group: Russia-Mongolia could play the role of suppliers of plentiful natural resources, Japan-ROK could provide capital and technology, and China could be a supplier of labor.

As for Russia, it was offered a "resource trap" model. At the beginning of the 1990s this "trap" seemed to be the natural means of integration of Pacific Russia with the markets of Northeast Asian countries, which was supposed would assist the inclusion of the entire Russian economy in this integration.

It is since 1991 that the general idea of the naturalness of the territories that surround the Sea of Japan (Japan, China, the ROK, the DPRK, Mongolia, and the Russian Far East) has been becoming a more real political and even economic fact. Nowadays, deep changes are taking place, forcing us to look at the processes which global civilization is undergoing in a new light. The common processes of the integration of the development of the world market economy influenced by globalization are becoming

objective economic forces bringing regional civilizations closer. It is extremely relevant in regard to the countries of Asia-Pacific, where active integration processes are observed, and the new center of world trade is being formed, with a unique culture, huge labor and raw-material resources, and a highly-developed technological base. At the same time, the specific intraregional problems that appear in the Asia-Pacific have a considerable influence on the development of international relations and the world economic system as a whole.

The financial and economic crisis of 2007-2009 has aptly demonstrated how great is the role of the key countries of Northeast Asia in the global economy. While by 2005 the US economy was consuming about 80% of all the surplus savings in the world economy,⁴ and constantly having huge trade deficits, the main portion of the resources that financed the US economy was created precisely in the countries of East and Northeast Asia, the leaders of which were China and Japan. In particular, they are the ones who finance the larger part of the US trade deficits. Recently, a system of "two engines" was formed in the world economy—one the gigantic balance-of-payments deficit in the current accounts of the United States and the second the currencies of East Asian countries that are rigidly-pegged to the dollar.⁵ These two macro agents act together in this system. The first is purely the exporter of final products and also the creditor, and the second is purely the importer and also the borrower. The typical macro agents of the first type are the economies of China and Japan, and of the second type the United States and Britain.⁶

Russia, which up to 2008 was also a pure creditor vis-à-vis the US economy, received additional confirmation of its potential membership in this "regional club." If Russia took into consideration the obvious potential membership in this club, however, the meaningfulness of that consideration would be limited to China, with which Russia has had complicated but much closer economic, trade, and political relations than with any other Northeast Asian country. At any rate, appreciation of the growing influence of the leading economic powers of Northeast Asia in the world economy makes Russia much more attentive to mutual activities with this particular subregion of the Asia-Pacific.

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² The most active authors of these concepts were K Kanamori, K Ogawa (Japan), Robert Scalapino, Lee-Jay Cho (USA), and Shi Min (PRC).

³ See, for example, Pavel Minakir, eds., "Economic Integration: Spatial Aspect", Moscow: *Ekonomika*, 2004.

⁴ "Surplus savings" refers to that part of the savings that is not invested in the economies that produce them.

⁵ N Roubini and B Setser, *Will the Bretton Woods 2 Regime Unravel Soon? The Risk of a Hard Landing in 2005-2006*, paper at the symposium "Revived Bretton Woods System: A New Paradigm for Asian Development?", Federal Reserve Bank of San Francisco, UC Berkeley, San Francisco, 4 February 2005; P Minakir and A Goryunov, *World Economic Crisis: Theoretical and applied aspects*, Vestnik DVO RAN, 2009, No. 4.

⁶ *Ibid.*

Northeast Asian Integration

Taking into consideration the size of countries, as well as differences in their economic and political systems, integration processes in Northeast Asia are developing according to a completely different model from the processes in Europe and North America.

Unlike the European Union, an example of classic integration, Northeast Asia, as well as the Asia-Pacific as a whole, does not yet have an official common customs union or any attempt at establishing a unified policy for regulating the process of integration. There exist inter-governmental bodies as well as business community associations, and the foundation of the integration process lies in the economic sphere rather than in the political sphere.

For quite some time the countries of Northeast Asia have demonstrated high rates of economic development, mainly due to China. According to experts from the World Bank, China (and partly Russia) will support rates of economic growth on a level above the world average in the forthcoming medium term.

Until the world economic recession (2008-2009), remarkable economic growth was possible due to the expansion of exports and the scale of the attraction of foreign investment. It became possible thanks to effective economic policies, which included the privatization and liberalization of national economies, as well as policies in the sphere of foreign trade and movement of capital. We can see, however, that there are substantial differences between the integration trends in the Asia-Pacific as a whole and Northeast Asia.

General frameworks for integration within Northeast Asia and the whole Asia-Pacific are connected to the realization of the so-called 1994 "Bogor Declaration" by APEC countries, which implies the creation of a free trade zone between the developed countries of APEC by 2010 and among all the members by 2020. This can support the economic dynamism of the region as well as the world economy as a whole in the mid- and long-term perspective.

Despite some difficulties, in 1992 there was formed a **free trade area (FTA)**, which covered the six founding members of ASEAN (the ASEAN Four plus Singapore and Brunei), but it does not have a comprehensive character either geographically or in terms of trade sectors. The goal of the creation of a geographically complete FTA to include new countries—members of ASEAN—was postponed until 2010, and the creation of a complete, comprehensive FTA *à la EU*, has been postponed until 2020. This movement also activated the process of the creation of a **Japan-China-ROK free trade zone**. The first step on this road has been taken: agreements regarding free trade for ASEAN-Japan, ASEAN-ROK, and ASEAN-China have already been concluded. More than that, bilateral and trilateral negotiations in search of optimal forms of subregional trade and economic alliances, and future cooperation, are being actively conducted.

These processes may have a significant geopolitical

effect partially due to the decrease in the influence of the United States in East Asia. According to calculations of Chinese, Japanese, and ROK experts, the formation of a trilateral free trade area in the form of NEA-3 will boost the combined GDP of Northeast Asia by 0.6%, Japan's GDP by 0.2%, China's by 1.3%, and the ROK's by 3.2%. Substantial effects are expected in the case of establishing free trade areas in the format "ASEAN + x". For example, calculations that were made by the ASEAN Secretariat demonstrate that the creation of a free trade area between China and ASEAN will increase the GDP of China by 0.3% and the GDP of ASEAN by 0.9%.⁷

The process of integration within Northeast Asia and between Northeast Asia and Southeast Asia has been ongoing since the early 1990s even in the financial sphere. Its first result was the signing of repurchase agreements between the central governments of eleven countries. According to the agreements, in the event of a financial crisis a country could exchange US treasury bonds for US currency kept in the central bank of another country participating in this arrangement. In the mid 1990s seven such agreements altogether were concluded at bilateral and multilateral forums:

- Indonesia, Malaysia, Thailand, Hong Kong, and Australia (1995);
- Singapore and Indonesia (1995);
- Hong Kong and the Philippines (1996);
- China and Hong Kong (1996);
- Japan, Australia, Hong Kong, Indonesia, Malaysia, the Philippines, Singapore, and Thailand (1996);
- The ROK, Australia, Japan, Hong Kong, and Singapore (January 1997);
- Hong Kong and New Zealand (March 1997).

The next step was taken after the 1997 crises, when Indonesia, Malaysia, Singapore, and Thailand concluded a "swap agreement" (ASA: ASEAN Swap Arrangement), according to which the central bank of the country in crisis could exchange its national currency for US dollars at the central bank of another participating country, with a commitment of buying back its currency after a certain period of time. At the same time Northeast Asian countries began to discuss a proposal regarding founding a development bank, the Northeast Asian Development Bank (NEADB). The main goal of the bank was to be assistance to the economic development of the countries and regions of Northeast Asia based on mutual cooperation.

Such integration processes occur mostly on a subregional level involving groups of countries that are sufficiently homogenous from the economic point of view and with a broad base of cooperation in different spheres. Without Russia's participation its closest geographical neighbors, China, Japan, and the ROK, have already begun forming approaches and mechanisms for future integration in Northeast Asia. They have created trilateral analytical groups which present coordinated recommendations to their governments in regard to tying together economic and financial policies, as well as the development of trade and

⁷ V Mikheev, "The East Asian Community: The Chinese Factor and Its Implications for Russia", Moscow: Moscow Carnegie Center, *Working Paper No. 1* (2004), p. 6.

economic cooperation between them.

In these countries, on the academic and business levels, such issues are being developed as: the creation in the region of a unified energy network and transport corridors to Europe (also through Russia); the formation of free trade areas; and a currency union.

China and Japan, however, are strategic competitors in the semi-conductor, steel, and other industries. Japan and the ROK are also divided by significant problems. In particular, both countries are eager to protect their inefficient agriculture and fisheries from competitive imports. Some old disputes between China and the ROK and Japan are not settled either. This can potentially slow down the creation of a free trade area in the form of NEA-3 because future partners are too apprehensive about one another.

The world financial and economic crisis that has been unfolding since 2007 has introduced significant changes to the estimates of the scale and form of the potential economic integration in Asia. From the point of view of Russia's participation in this process, however, there have been no considerable changes.

Russia: A Player or a Spectator?

What do all these processes mean for Russia today and in the future? What kind of economic policy vis-à-vis the countries of the region should Russia pursue? In formal terms Russia participates in the work of integrative construction in Northeast Asia. In reality its role is limited by trade activities. Meanwhile, even in the trade sphere, the Northeast Asian countries up until now have been enjoying a limited role as Russian economic partners (Table 1). As of 2010 just 16% of the total trade turnover of Russia was connected with Northeast Asian markets. At the same time this share has doubled since 2000. It means that the general strategy of filtering through to Northeast Asian markets is going successfully enough due to the appearance of very new components in trade between Russia and Northeast Asian countries. These components are not oil and gas, but import goods. For example Russian exports to Northeast Asia increased 4.4 times in the period 2000-2010 (from US\$9.5 billion to US\$44.5 billion), yet Russian imports from Northeast Asia during the same time period increased 29 times (from US\$1.9 billion to US\$56.7 billion).

Of course the role of foreign trade with Northeast Asian countries is much more sufficient in the case of the

Russian Far East. As of 2010 the share of the Russian Far East trade turnover for Northeast Asia was 86% compared with 67.3% in 2000. In this case the main role in the growth of trade interdependence was played by imports which increased 13.6 times in the period 2000-2010 (from US\$0.4 billion to US\$5.6 billion), while the increase in exports was 5.8 times (from US\$2.5 billion to US\$14.6 billion).

At the same time a thesis about the particular role of the Russian Far East as a base for the integration of the entire Russian economy into the Northeast Asian rim is not confirmed in the case of foreign trade. The share of the Russian Far East in the foreign trade turnover of Russia with Northeast Asian countries is only 3.8%, growing slightly over the last decade (3.3% in 2000).

The interdependence between Russia and the Russian Far East on the one side and Northeast Asian countries on the other is minimal. As of 2010 the total volume of investments from the NEA-3 (China, Japan, and the ROK) to Russia was US\$10.6 billion and to the Russian Far East US\$0.9 billion, or 9.2% and 12.3%, respectively, of the total foreign investment turnover of Russia and the Russian Far East. Asian capital has still remained reluctant to enter the Russian market. About 80% of the total volume of investment and of direct investment is coming from Europe (Cyprus, Britain (including the British Virgin Islands), the Netherlands, Germany, Luxembourg, and France).

Theoretically, taking into consideration that integration interactions in Northeast Asia are characterized by being at a considerably lower level than in Southeast Asia, Russia still has a chance to undertake active participation in the formation of the new architecture of this integration.

In fact, despite all the efforts that were undertaken by Russia over the last 5-6 years to gain access to Asian markets in goods and services, as well as capital markets, the results still do not match the expectations. Partners in East and Northeast Asia still perceive Russia almost exclusively as a supplier of raw materials, and in this regard the Russian Far East is perceived as a transit territory that serves for transport corridors to supply those resources. Further, Russia encourages Northeast Asian countries to maintain these positions by pursuing the target of being a part of the Asian economic world on the basis of the construction and development of transport and energy transit corridors through the Russian Far East.

To date, the economic integration of Russia with countries of Northeast Asia is almost exclusively determined by hopes to create international transportation infrastructure and international fuel energy structures in the

**Table 1: Foreign Trade Turnover between Russia and Northeast Asian Countries
(US\$ million / % of the total trade turnover of Russia)**

Destination	2000	2008	2010
China	6,213.8 / 4.8	56,145.5 / 7.7	59,334.0 / 9.6
Republic of Korea	1,458.9 / 1.1	18,956.4 / 2.6	17,683.7 / 2.9
Japan	3,536.5 / 2.7	29,223.1 / 4.0	23,080.2 / 3.7
DPR Korea	46.1 / 0	111.1 / 0	62.3 / 0
Mongolia	222.8 / 0.2	1,169.6 / 0.2	1,015.4 / 0.2
<i>Total Northeast Asia</i>	11,478.1 / 8.8	105,605.7 / 14.5	101,175.6 / 16.4

region. The strategy of support for Russia's and individual companies' efforts to be included in the economic processes in the Asia-Pacific is based on the common idea of the formation of infrastructure relating to international economic integration. Such infrastructure, according to analyses in the 1990s⁸ and also according to the beliefs of contemporary Russian bureaucrats,⁹ should first be a system of alternative transport corridors passing through the territory of the Far East of the Russian Federation, and second a systemic energy infrastructure connecting the eastern territories of Russia and energy markets in the countries of Northeast Asia. The idea is that joint systems of transport corridors and energy infrastructure will create a T-shaped body which will serve as a foundation for the scale and structure of diversified integration cooperation.

The realization of these projects particularly intensified after 2005, based on the considerable financial resources accumulated as a result of the rise of the world prices for oil, natural gas, and other raw material export items. In 2007, the financing of activities related to the program for the development of the Far East and Zabaykalye was increased significantly in connection with the decision to host the APEC summit in 2012 in Vladivostok.

Objectively, such a strategy of "market-creation

integration" connects up with the general direction of establishing a "Russia-World" model by the economically developed community. Russia is evaluated by the world economic community to be a potential dangerous competitor. That's why the common interests of this community are firstly to limit Russia's competitive advantages in foreign markets through supplying competitive products with a high degree of processing, and secondly to fix Russia's position in the international division of labor as a raw materials supplier.

There are two paths for Russian economic cooperation with the Northeast Asian community:

- 1) Following the strategy of "commodity market" construction and the fixing of the "external resource supplier" viewpoint regarding the future Northeast Asian + ASEAN integration community.
- 2) Trying to be included, at the political and economic level, in the process of economic, technological, financial and institutional integration and to become a part of the future integrative community in East Asia.

The effects of the possible choices are evident both for Russia and for Northeast Asia. But what choice will be made by Russia and by the NEA-3?

⁸ See, for example, Pavel Minakir and Victor Ishaev, *The Far East of Russia: The Problems and Possibilities of Economic Development*, Vladivostok: DVO RAN, 1998.

⁹ See, for example, Project "Strategy of Social-Economic Development of the Russian Far East, the Republic of Buryatia, Zabaykalsky Krai, and Irkutsk Oblast for the Period to 2025", 12 May 2009, prepared by the Center for Strategic Research (Moscow) for the government of the Russian Federation.