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## RUSSIA'S EASTWARD TURN: EXPECTATIONS AND DISAPPOINTMENTS

A series of geopolitical conflicts between Russia and the West makes it seem that Russia should inevitably turn to the East, i.e. change its political and economic benchmarks and

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partners. The "window to Europe" cut by Peter the Great is being tightly sealed in anticipation of a long "winter" in Russian-European relations. There is an urge to widely open the gates to the "warm" Asia-Pacific region, first of all to China. The Russian elite has demonstrated euphoric expectations – China will replace Europe as a buyer of our raw materials, a source of technology and investment.

The reality is much harsher. China is slowing its development and is not generating a growing demand for raw materials, is very selective in the development of projects, seeks to ensure a cheap raw material base and does not want to create itself a competitor. The Asia-Pacific Region (APR) is emerging as a hub of new opportunities for strengthening economic and geopolitical competitiveness. Without their clear understanding, the pursuit of phantom benefits from the change in global orientation will result in a few lost years at best, and in decades on the sidelines of world development at worst.

What is Russia's strategic national interest? This is not integration for its own sake, not just friendship and trade. Russia's imperative today is reindustrialization. The stake can be placed on agriculture, eco-tourism and sale of clean water, but it would require a complete reboot of the national character. Commodity specialization is a short-term strategy, which should be followed either by a sprint into industrialization, or an exit from the circle of leading world players with no chance of survival after the depletion of natural resources. The idea of a "great leap" into the post-industrial era without an industrial foundation is downright utopic.

### The alluring East

The concept that the twenty-first century will be an "Asian century" has become commonplace. China became the main locomotive of development, with an average annual growth rate of 10.5% between 2000 and 2010. Back in the early 2000s, it was logical for Russia, given its place in the global division of labor, to develop ties with countries of the Asia-Pacific region and actively enter local markets. However, Asian countries have not been of great interest to Russia for quite a while. Until 2011, there were no pipelines linking Russian subsoil with Asian consumers.

2009 can be considered the beginning of Russia's eastward turn. When commodity prices fell, the usual sources of funding in the West temporarily dried up, and the resources of the Russian government appeared to be limited, many companies turned to Asia in search for new sources of capital. Among the most significant achievements is the signing of a contract between Rosneft, Transneft and CNPC for the construction of the Skovorodino-Mohe branch of the Eastern Siberia-Pacific Ocean (ESPO) main oil pipeline. Under the terms of the contract, in exchange for a \$25 billion loan from the China Development Bank, Russian companies agreed to supply 15 million tons of oil to China annually for 20 years. Another landmark event was Rusal's IPO at the Hong Kong Stock Exchange in January 2010.

Finally, in the spring of 2014, the "turn" was continued under the influence of the events in Ukraine. 42 agreements were signed in Shanghai, the most important of which was the gas contract between Gazprom and CNPC on the construction of the Power of Siberia gas pipeline, valued at \$400 billion back then.

### Russian vision of the "Asian course"

Russian vision of the "Asian course" was super-optimistic and consisted in the idea that within 10–15 years, Russia would be able to balance the shares of trade with the EU and the APR in the trade turnover to such an extent that a further split in trade relations with Europe would not cause unacceptable damage to the economy. The flow of

Asian investment will replace Western investment, albeit not completely. China will become Russia's main partner in Asia; Russia's relations with it will follow the same pattern as with Europe: Russian raw materials in exchange for loans, technology, and investment. The steadily growing demand for energy, metals and fertilizers in China will create a powerful incentive for the growth of the Russian economy. A lot of money will come from the Asian Infrastructure Investment Bank and the Silk Road Fund. Southeast Asia will become a market for domestic mechanical engineering products and infrastructure solutions.

As the past years have shown, this vision was not realistic. Russia needs to rethink the "Asian vector" of its foreign economic strategy.

Today Russian politicians and experts are surprised by the "unfriendly" actions on the Chinese part: closure of the Chinese skies for airplanes with "double registration" (re-registered in Russia without the lessors' consent), intention of Chinese companies to withdraw from the Arctic LNG-2 project, termination of Huawei contracts with Russian operators for the supply of network equipment. This contradicts our picture of the world where there are two centers of power – the United States and Russia, and the rest must decide who to join. We perceive the political and economic contradictions between China and the United States as no-alternative Chinese support for Russia without taking into account the historical and cultural background of the Chinese nation.

At certain points in its history, China produced nearly 50% of the world's GDP and was hundreds of years ahead of other nations that it perceived as barbarians and of no interest to the Middle Kingdom. China perceived itself as the center of civilization, its emperor as the ruler of the whole earth, and the other countries as his tributaries. It was not until the middle of the nineteenth century that China had established a foreign ministry when "barbarians" from the West started coming to the country. The name of the ministry spoke for itself: "The Ministry for the Administration of the Affairs of All Nations." A country with such a worldview would not be a guided "faithful vassal." China is pragmatic and has its own interests at heart, and it's up to you whether or not to go along with it. Chinese political scientists and experts in international forums directly state that the fate of the world depends on relations between the United States and China. It is naive to expect China to be willing to break ties with its main consumers, the EU and the U.S., for the sake of "solidarity" with Russia.

In the current circumstances, pursuit of the "Asian vector" of Russia's foreign economic strategy is fraught with significant difficulties and will not replace ties with the West in the medium term. The development of ties with Asian states and work with regional investors is belated and occurs in an extremely unfavorable external environment. The specific problems to be considered for successful integration in the Asia-Pacific region include several challenges:

- moving away from an exclusive focus on China;
- reducing the negative impact of sanctions;
- building knowledge about Russia among Asian investors, as well Russia's expert knowledge of APR (including government, business and civil society).

Structural reforms and radical improvement of the investment climate in Russia will be a prerequisite for success.

### The dawn of industrialization

It would be useful to recall how industrialization occurred in the Soviet Union. Whence, as if by magic, heavy industry arose in an agricultural country and nearly completely technically prepared it for a long war? The history textbook never told us about American citizen Albert Kahn and his prominent role in Soviet industrialization. Famed as “Ford’s architect,” Albert Kahn was invited to the USSR, prepared an industrial construction program, and in 1930 received a contract to organize the construction of industrial plants to the equivalent amount greater than the current annual federal budget. His firm designed and organized the construction of more than 500 plants. Dozens to hundreds of American and German firms worked on all the sites, performing all kinds of work, from design and construction to equipment supply. It was all paid for with currency from grain shipments. The village bore the burden of industrialization on its shoulders and broke its back.

Today it looks like absolute fiction. On the one hand, there was absolute ideological intransigence, no match for the current one. On the other hand, there were economic interests, the Great Depression, and the pragmatic approach. All of this is no reason to dust our heads with ashes and indulge in a feeling of “national humiliation.” If you think carefully about it, it was the only possible option for obtaining high technology and equipment for accelerated industrialization. Where would we be in 1941 if supporters of “total import substitution” had won?

### Industrialization, take two

Today it is both easier and more difficult to launch industrialization in Russia. On the one hand, there are no irreconcilable ideological contradictions with the outside world. On the other hand, strong competitors have risen to occupy the niche of factories of the world – Japan, China, India, and other countries of the Asia-Pacific region.

There is a great temptation to go into isolation under the slogan of “self-reliance,” to close ourselves off from competition. “Buying your own” is a good thing, but it can’t be worked out overnight. Raw materials, components, equipment, and technology will have to be purchased for foreign currency for a long time to come. Where do we get the currency? We should develop industries that produce goods for export in addition to minerals. For example, agriculture, computer technology. Import substitution is the development of export industries, not the closure of the domestic market; this way we will only mothball technological backwardness.

Where can Russian industrial products be in demand, besides the domestic market? Where do we get the technology, the equipment, the investment? Our natural partner is, again, Europe, in its post-industrial part. Just as China is now the industrial factory of the United States, so Russia can compete for the place of the industrial factory of Europe without giving up on the CIS market. Entrepreneurs in the 1990s naturally came up with this solution. The authorities and the business community faced the non-trivial task of combining Russian entrepreneurship, Western technology, and a mostly Central Asian workforce to carefully cultivate a new industry on the rocky domestic soil.

What were Russia’s historical advantages? First of all, its cultural and territorial proximity to Europe. Europe and Russia together are able to create a self-sufficient conglomerate – from raw materials to post-industrial goods, with

a gradual shift of the industrial component to the East. If the “national pride of Great Russians” does not allow us to pursue the same path as Peter the Great, then we are left with the option of a raw materials appendage of China, or whatever you call it. The Chinese are not objectively interested in creating a competitor on the China-Europe line for themselves; Russia, in economic terms, may be of interest to them as a source of cheap raw materials and a territory for transport links. Should we develop economic ties with China and the Asia-Pacific region as a whole? Yes, absolutely. But we should not expect a free of charge “Oriental miracle.”

### The window of opportunity is closing

We must clearly understand that our advantages are melting away, we have very little historical time left. China is rapidly mastering the best business practices and modern corporate governance. The country is becoming a global player, so that when we turn to the East, we will be astonished to find the same Westernized approaches that sometimes exasperate our authorities so much. China has also embarked on elimination of its second disadvantage, its remoteness from Europe. If the economies of Europe and China connect via a transport corridor for rapid delivery of goods, Russia will be left with a very modest place in the global division of labor. The reward is a transportation tariff and a lack of economic future, that is, of a historical perspective. The Silk Road will turn into a ring of steel.

Reindustrialization in our country has been actively pursued until it was swept away by the hurricane of oil and gas revenues. The country’s elite and citizens alike believed in the eternal happiness of oil and gas rentiers. In the foreign policy, the “superpower” motifs resounded again. It is already clear that the world does not want to rebuild itself according to our recipes, and foreign policy projects are beginning to press the Russian economy down.

In the spirit of the new direction of thought, let’s harken to the East. Deng Xiaoping willed China to keep a low profile and not demonstrate its claims to leadership. China’s exclusive focus on internal development, the desire to avoid any conflicts that might interfere with it, has produced phenomenal results. Only a foreign policy that creates the best opportunities for the internal development of the country can be considered effective.

In view of the revealed limitations of the Far Eastern track, the turn toward the Asia-Pacific region is increasingly impeded by the need for structural reforms in the all-Russian economic space as a whole. This is also the starting point of a long-term strategy for the new positioning of Russia in the global economy, capable of producing positive results.

Foreign policy initiatives will have to be aimed not only at easing current tensions with the West and lifting sanctions regimes, but also at creating and strengthening international guarantees for a conflict-free transformation of the global economy.

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