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Realizing Russia's Potential
STRATEGIC DEVELOPMENT OF EASTERN SIBERIA AND FAR EAST AND
POTENTIAL INTEGRATION WITH PAN-ASIA MARKETS
Arena Debate

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In cooperation with En+ Group

Moderator:

Mark L. Clifford, Executive Director, Asia Business Council

Panelists:

Oleg Deripaska, President, En+ Group; Chief Executive Officer, Chairman of the Management Board, UC RUSAL

Vladimir Dmitriev, Chairman, Bank for Development and Foreign Economic Affairs (Vnesheconombank) state corporation

Ling Wen, President, Chief Executive Officer, China Shenhua Energy Company

Vladimir Yakunin, President, Russian Railways

Bong-Jin Yang, Chief Executive Officer, Hyundai Energy and Resources Ltd.

Front row participants:

Vladimir Miklushevsky, Governor of the Primorsky Krai

Vadim Shvetsov, General Director, Sollers OJSC

Andrei Slepnev, Member of the Board on Trade, Eurasian Economic Commission

M. Clifford:

Good afternoon, everyone. Thank you for your patience. We are starting about 15 minutes late so we will finish 15 minutes later. We will finish promptly at 17:30. My name is Mark Clifford. I live in Hong Kong. I am the Executive Director of the Asia Business Council.

It is my great pleasure today to help moderate a panel that I think is exploring one of the most important issues facing Russia, and also Northeast Asia; that is the problem of how to pull together the tremendous natural resources of the Russian Far East in Siberia, and to marry them to the vast demand in Northeast Asia.

The challenge is simple. Most Russian resources are in the eastern two thirds of the country, in Siberia, in the Far East. About 70% of the natural resources are there. But most Russians live in the west. More than 80% are in the European part.

Of course, those resources are next to the dramatic, fast-growing Asian economies. There is a new Ministry for Far East Development, and President Putin has a special panel that is due to forward recommendations to him by July 1, 2012 on how best to tap these resources. There are a lot of ideas around and I can hardly think of anyone better than the panelists we have to talk about how to move forward.

Let me start with Oleg Deripaska. You have been at the centre of the attempts in Russia to move forward in terms of developing these resources. What needs to be done?

O. Deripaska:

First of all, it is imperative to define the aims of development of our territories of Eastern Siberia and the Far East. These aims must be balanced. First of all, we must meet the demand which is growing in both the European part of the country and the Urals, to restore potential and to become a major engineering base. Secondly, we need to implement the accelerated integrated development of our territory, using the potential demand of Asian markets.

The question is, how do we balance flows and define priorities for the development of natural resource deposits? It is impossible to solve these problems without

developing ports. The combined capacity of our ports today is a little less than 115 million tonnes, and the combined capacity of our overland haulage is less than 62 million tonnes. For growth, we need to double, or even triple potential export capacity, ensuring at the same time the corresponding possibilities for infrastructure as a whole: railways, energy infrastructure, and the creation of gas infrastructure.

The paradigm for financing and investment expenditure must be changed. The old concept for ensuring infrastructural development at the expense of tariffs is not possible, because it limits the speed of growth. We need to pay attention to the suggestion of Yevgeny regarding increasing the volume of loans, taking into account the capacity of the Pension Fund of the Russian Federation. These resources must be made accessible for the development of infrastructure, for a total of USD 180–200 billion.

After that, we need to solve the problem of developing the financial infrastructure. The quantity of banks and financial institutions in that part of the country has shrunk by two thirds, even when compared to 2002 and 2003. From one perspective, this is good – the reliable institutions have remained. On the other hand, we have entirely transferred the financial potential into the European part of the country, which impedes the development of social and business infrastructure.

A whole series of problems are awaiting solutions: the creation of a regional aviation industry; the creation of a regional transport network system, including highway services; the improvement of checkpoint and customs control operations; and significant integration with Mongolia, a territory that will receive maximum benefits from the development of infrastructure in Eastern Siberia and the Far East.

It is very important to determine a methodology for access to resources. We often hear about the limitations, but it is imperative for us to understand that there are no limitations today. In several examples of natural resources deposits we have seen the following pattern: a company acquires the deposit, and then this becomes a bargaining chip in the competition for venture investment. The deposit is passed from one hand to another without a programme for development, without an integrated programme for exploitation, and in the end, the cost of its development

grows and the potential attraction gets lower. There is a need to clearly define regulations. There is no need to redistribute licenses, but it is necessary to bring some clarity to the process. Many licenses are renewed from year to year, while the state of the resource deposit does not change. There is a need to elaborate on the regulations that determine the procedures and timetables for project construction necessary for the development of resource deposits, and timetables for the creation of social infrastructure objectives.

An important question is how to finance infrastructure objectives. We have good experience in this area. We undertook a development programme of the Upper Angara Region, with the assistance of an investment fund, in 2005–2006. In compliance with this programme, decisions were made concerning the construction of a hydroelectric power station and an aluminium plant. I believe that this experience was revolutionary for Russia. Since that time, the budget has been increased by 6% in total. We have gone through the crisis of 2008 and 2009 and deviated from the initial launch timetables by only nine months, taking into account all the difficulties connected with finalizing the project documentation.

The practical aspects of a public-private partnership have already been worked out, as has practical financing activity under this partnership. The construction of infrastructure has also been worked out in advance. We see that there is the question of attracting the necessary manpower resources for the implementation of projects, which need to be looked at in the context of the problem of workforce migration.

M. Clifford:

Thank you very much, we will come back to this issue, infrastructure. What are the priorities in finance, how are we going to pay for it?

Let us switch. We are lucky on this panel, because we have participants from China and Korea. Zhang Cheng, you have a joint venture with Oleg Deripaska to do hydropower. Maybe it will be the biggest hydropower operator in the world in some years to come. What is the attraction for China, as far as you are concerned?

Z. Cheng:

We know that the Russian government has confirmed an entire dedicated programme of development of the Russian territories of Eastern Siberia and the Far East, opening up the opportunity for the collaborative development of many resources.

We think that in the Far East region, as a priority, the energy sector should be developed, based first and foremost on renewable energy sources. Hydroelectricity is one of these priorities. The development in this area will ensure dynamic growth of the economy of the entire vast region and the development of the territory. We have significant joint experience working with RusHydro. Collaboration must take place based on transparent foundations, on a long-term basis, and with the rational management of risks that occur in the joint development of resources and territories. Our company actively participated in the implementation of the Three Gorges Dam project in China. This experience in constructing a first-rate hydroelectric facility was unique, and this background can be used in the strategic development of Eastern Siberia and the Far East. Participation in the project allowed us to train enormous numbers of personnel and get acquainted with the equipment. As such, we have both the experience and the financial resources for participation in the development of Eastern Siberia and the Far East. We are sure that we will succeed in moving forward.

Thank you.

M. Clifford:

Thank you. Let us get another perspective from China. Wen Ling, you are very interested in the coal sector. What does Russia have to offer?

Ling Wen:

Thank you, Chair. It is a great honour for me to be here, and it is also the first time that China Shenhua Energy has been able to attend this Forum.

Let me first introduce Shenhua Group very briefly. We were established in 1995, so we are a very young company, but by last year we were the largest coal producer globally. In terms of coal production volume, we had more than 400 million tonnes, and a total sales volume of 500 million tonnes. We also have a long distance railway, much shorter than yours, but we have more than 1,600 kilometres. We are the sixth largest IPP in China. In terms of total in-stock capacity, we have more than 60 gigawatts. So, we have the harbours and total capacity, we have more than 130 million metric tonnes. We also have a very special sector, coal to liquid and coal to chemical. Coal to liquid means transferring the coal directly into oil, diesel, and gasoline.

Talking about cooperation between all our interests in the Russian Far East area, the number one thing is, I think that cooperation between Russia and China is a very good thing, because now with the development of the Far East and Siberian area, China also has a policy on the development of Northeast China. So the combination is very similar.

In talking about potential cooperation, the main point is that in Russia, you can develop a large amount of energy in this area: oil and gas, coal, power, etc. But the greatest demand for energy comes from China.

The second point is, at Shenhua we have a syndicate business model. We have coal, railway, power, coal to chemical, and coal to liquid. So we can forge cooperation here, for example, we can make some developments in coal mines. We are very good at underground coal mines and open pit coal mines, and also we can cooperate with my friend, President of Russian Railways, Mr. Yakunin. Actually, we are discussing potential cooperation not only in Russia but also in a third country, Mongolia, and other opportunities.

The third matter is that we have the option of engaging in coal production here for long distance transportation to the Asia-Pacific region. We can also generate the power here first, and then use long distance transportation through the grid system. Also, we are talking about potential ways to transform coal into oil and gas, and also

chemicals, and make the transportation costs much lower than for coal. So we have a lot of interests. Thank you.

M. Clifford:

This all sounds great, but I would like to turn to B.J. Yang, because Hyundai has been trying to put what looks fantastic and almost simple on paper, into practice. Hyundai has been working in Primorsky Krai and other parts of the Far East in Siberia for over 20 years. As a matter of fact, one of Dr. Yang's predecessors is now President of Korea. I think there is a lot of familiarity with doing business in this part of the world. So, how does it look on the ground?

Bong-Jin Yang:

Thank you, Mark. First of all, I would like to apologize. My voice is almost gone after an exhausting flight from Seoul to here. But, I would like to talk about adding to Oleg's summary of macro issues relating to the Primorsky Krai.

He mentioned some balancing activities between Europe and the eastern area, but I think that it is the right time for Russia to put more emphasis on the east rather than Europe. If Peter the Great lived today, I think he would have built a third capital here, on the eastern side, rather than somewhere else, because APEC countries account for at least 60% of the global GDP. So, that highlights why the eastern side is so important in the Russian economy. And as Oleg mentioned, it is inevitable and indispensable that rail and port infrastructures should be built as soon as possible to accommodate economic growth and prosperity on the eastern side.

Let me introduce my company, as Mr. Wen Ling introduced his company. Hyundai's founder has had an interest in and commitment to the Primorsky Krai since before the diplomatic relationship was established between Russia and Korea. He first studied lumber loading there, but it was not very successful. He was also interested in exploring the oil and gas business together with Russian partners, but the lumber business killed his ambition and he pulled out. But he maintained a hotel in Vladivostok, which is one of the most luxurious hotels to the east of the Urals, and

now more hotels are springing up in Vladivostok. But, we still maintain our Hyundai hotel there.

We are building a new GIS plant near the Vladivostok area. We opened two farms in Primorsky Krai about four years ago. We took this over from a New Zealand company. I think it is going quite smoothly, and we want to expand as extensively as possible, if the Governor sitting here allows me to have more land. We imported a lot of agricultural machinery from the United States, and I think we are doing quite nicely so far.

But one thing I would like to point out is that the speed of doing business is very different. In Korea, you are talking about doing business at the speed of light, which is what the digital age is all about. In Korea, if you move from place A to place B, you wake up in the morning in the same bed, but after moving the bed to a new place, you can sleep in the same bed as you did in the morning. That speed is what is needed in Russia now. I mean, we moved an office from Vladivostok to Ussuriysk for agricultural farming. It took us almost two and a half months to establish the office before the Internet, gas, electricity, and registration with the appropriate government authorities and so on were completely taken care of. So the speed is too slow in Russia.

I think that management of speed is very important for accommodating new trends in the eastern side. China, Japan, and Korea have the same speed but Russia is very slow. That has to do with the taxation, bureaucracy, and all kinds of red tape involved in the permit process. I think that has to be reformed as soon as possible.

M. Clifford:

Thank you very much. Vladimir Yakunin, you run the rail system, one of the most impressive in the world, but also one that needs much more capacity. To Dr. Yang's point, what are you going to do? How fast can you do it? What is needed in the Far East and in Siberia?

V. Yakunin:

Following the example of my colleagues, I would also like to introduce our 'little-known' company. It is one of the biggest companies in the world. About 1.1 million people work for us. We are currently undergoing reform. We have the best investment rating in Russia from the perspective of investment agencies. This standalone rating allows us to attract monetary resources under the most beneficial conditions. As such we have well-reasoned arguments when dealing with the experts who still announce that companies belonging to the state function less effectively than companies that remain in private hands. I think that Mr. Deripaska will have to agree with me in this regard.

As regards the issues under discussion, I can confirm that the development of infrastructure is a priority. Mr. Deripaska and my friend Mr. Wen have just spoken about this. The solution to this problem is particularly necessary for the development of the territories beyond the Urals: Siberia and the Far East.

I fully agree with what Mr. Deripaska has said just now, that it is impossible to count on the endless raising of tariffs for the creation of investment resources for the development of infrastructure. I can cite the experienced of developed countries. In the US, money belonging to the government makes up 54% of general monetary circulation. In European countries, state funds makes up 35–37% on average. In Russia, the share of these resources is about 27%. When we talk about the withdrawal of government from the management of the economy, we need to bear in mind what is hidden behind this. I was inspired by President Putin's announcement about utilizing the accumulation of the Pension Fund in the interests of developing infrastructure and the creation of infrastructural bonds.

It is obvious that infrastructure must be developed at a faster pace than the economy. I would like to explain this view with a concrete example. Regarding the changes to the situation of global economic markets, the volume of goods that we transport to Far Eastern ports has risen by 32% since 2007. By the calculations of our specialists, the total volume of commodity circulation along this chain should grow by 40% by the year 2020, and in the Far East region, it should grow two and a half times. We are working with the government and we have already presented our

suggestions for the development of infrastructure. I can cite some figures regarding these suggestions: to ensure economic demand in the transportation of goods and passengers, about RUB 181 billion is needed for the modernization of the Trans-Siberian Railway, and about RUB 787 billion is needed for the modernization of the BAM as a main freight artery.

We are collaborating closely with our Chinese colleagues and are working energetically. We are conscious of the fact that developing these regions offers progress in our cooperation with China. Not long ago we signed a special agreement on the creation of an integrated logistics company, which will conduct the transportation of goods from China to Europe and in the opposite direction. This agreement was reached between the western Chinese province of Chongqing, Kazakhstan, and German companies. As a whole, we are proceeding from the need to develop cooperation with those companies that are investing in Russia. I very much liked what Mr. Wen noted in relation to the possibility of processing coal on site, converting it into products for chemical production, which has a higher added value. Such technology is necessary because in the current conditions we must cover 4,000 kilometres in either direction to transport coal from the Kuznetsk basin. This limits the competitiveness of the coal industry and of the economy in general. It is imperative that we expand our collaboration with Mongolia as well. We spoke about this not long ago in Beijing during President Putin's state visit. On our part, we are ready for such a collaboration.

I think that today the collaboration in the development of the Far East region and Siberia could satisfy mutual interests in the implementation of cluster projects with the participation of foreign investors. However, I can cite one negative example. I worked very actively with the Japanese Embassy and visited Japan on more than one occasion after my appointment as President of the company. We often conducted discussions about the possibility of Japanese investment in the Far East region. More recently, I have not been traveling to Japan. Why? It was clear to me that after the tragedy that occurred with the nuclear power station, it was necessary to try and organize collaboration with Russia. As Mr. Deripaska noted, coal

resources are now accessible. It was necessary to construct a power station, to use this coal on site, and to export the needed electric energy to Japan from Russia. However, this did not happen, even with all the good intentions from the Russian side, which only strengthened after the tragedy.

It seems to me that we are underestimating something, and are falling short somewhere. By all appearances, state governing bodies are not quick enough to take advantage of the opportunities that they possess. The development of the Far East and Siberia is practically impossible without the development of infrastructure, and in particular railways. I hope that the suggestions I have presented today at this plenary discussion and the plans formulated by our government will absolutely be developed further. We are absolutely open to collaboration with business, because we do not produce goods ourselves, but provide a service in the transportation of goods. The development of a real economy for both Russia and for the whole Eurasian territory is critically important for us, as we are carrying out exactly this kind of policy in the field of transport corridors.

Thank you.

M. Clifford:

Thank you, Mr. Yakunin. I have a follow-up question – just a quick answer please. If we come back here in ten years and have a similar session, will people still say that there is not enough rail capacity in Siberia and in the Far East?

V. Yakunin:

If a decision about the production of infrastructural bonds is not taken, government investment in infrastructure will not be added on to. I am afraid that then we will be talking not about inadequate capacity, but about completely different factors.

M. Clifford:

Speaking of money, let me go back to Oleg Deripaska. You have been among the most outward looking, certainly the business group that is looking the most to China.

You had the IPO in Hong Kong, the Rusal IPO, the first Russian company, I believe, to list in Hong Kong. I think you just lined up some money from the Chinese Export-Import Bank. Is China going to be a more important source of funds for your group and for Russia more generally, especially for the development of the Far East and Siberia, and is that a good thing, a necessary thing?

O. Deripaska:

As has been said, China is, without question, a very important partner. Siberia is not only important for Asia, it is also significant for Russia. Mr. Yang tried to correct me, insisting that we need to look more to the East, but I was talking about the European part of the country. We will develop resources, taking into account the potential demand that exists in China, Korea, Japan, and other countries of Southeast Asia. The large availability of resources for the development of our engineering base creates many advantages for us. China is Russia's fastest growing partner.

The level of cooperation is also determined by the level of collaboration between our countries in the political sphere. Solutions to the problems connected with border areas, solutions to the problems with the first phase of oil deals and contracts, the imperative solution on the question of gas: all of this allows for the development not only of political relations between Russia and China, but also of our business relationships.

We have started to understand each other better. We better understand now what Mr. Wen was saying about the necessity for the construction of power stations within Russia. We can provide deliveries of aluminium to China, which is also a power-consuming material, but it is not always necessary to transfer the base load to China. We can solve many problems by constructing a power station on Russian soil and by developing the raw-material potential and the next stage of its reconfiguration. I believe that we need to look at the development of territories as a whole, taking into account the interests of all sides: Russia, China, Korea, and Japan.

I would like to talk a little bit about the residents of this region. Siberia is a unique part of Russia with its own character. Siberian troops saved Moscow during the Second World War. The development of a common infrastructure is important to accelerate the implementation of projects, as Mr. Yang said. The improvement of the general infrastructure includes the development of airports and train stations, the increase of passenger and railway networks within the territory, the construction of hotels, the modernization of universities and technical colleges, raising the quality of medical services, and solving questions related to telecommunications. The Ministry for Development of the Russian Far East was created to fulfil these tasks. Other issues were also discussed, such as whether the need exists to create a corporation capable of solving the problem of insufficient investment in the critical areas of social and business infrastructure. Accelerated development of the territory is impossible without the creation of social and business infrastructure. This is also very important. We will build roads and ports and the situation will be improved. For that very reason, questions arise: will we be capable of creating new conditions for the inhabitants of the region, of ensuring jobs for them, and ensuring a quality of life which will attract people to go there? Will we be capable of developing the territory from the perspective of raising the general level of prosperity?

M. Clifford:

Let me come back to you on China. I have a sense, as a visitor who is not that familiar with Russia, that there are people who are uneasy about embracing China, both in terms of investment, and especially in terms of Chinese money coming in, whether it involves working with groups like yours, or buying up resources. How do you reassure your fellow Russians that China is an ally, and not a threat?

O. Deripaska:

I was talking about precisely that. The crux of the matter is not in the selling of resources, but in the development of the territory. If the inhabitants of Siberia see that development is taking place simultaneously with trade, they will not have any

doubts. They will understand what benefits are presented by attracted investment. I do not agree that there is prejudice against investment from China. It is possible that that is a European point of view: that Russia and China, and Russia and Asian countries must necessarily come into conflict. This widespread opinion does not reflect reality. Russia and China, and Russia and Asia will never be in conflict. Russia is Asia with a European face. Russia is the bridge between Europe and Asia.

M. Clifford:

Tell us a bit more from the Chinese side, Yang. Should Russia be afraid? I mean you have a lot of people in China, and not too many people in Russia. People seem to think that somehow China is going to come in and take possession of Russia's East. Should people worry?

L. Wen:

I want to say that our collaboration is not a relationship based on struggle, not a relationship of competition, but a relationship of cooperation. First of all, Siberia and the Far East must develop – people need jobs, and markets for the production of Siberian and Far Eastern products exist in China, Korea, and Japan.

Secondly, our cooperation is built on the principle of mutual benefit. Russia can receive technology from us, as well as capital for the development of the mining sectors, and it can build its extraction and manufacturing industries. There is no contradiction here. On the other hand, for a businessman, this is just business.

M. Clifford:

I agree that business is business, but I feel that on paper it seems so simple. Why does it take so long for this cooperation to develop?

L. Wen:

The Chinese do not think that relations with Russia are bad. On the contrary, for us Russia is a very good neighbour. As they say, a close neighbour is much better than a distant relative. If you ask about relations between China and Russia and between China and America, the majority of Chinese people will say that relations with Russia are more important and better than those with America.

Thank you.

M. Clifford:

I am just curious. Maybe Bong-Jin Yang could help us. Again, I think business relationships are very important for building trust between countries, and it seems that one of the things that Russia and China would want to do to build greater trust, is accelerate business activities and business investment. What can be done by us and the governments to push things forward faster, so that in ten years from now we are not still talking about why things are so slow?

Z. Cheng:

This is a question of shifting the paradigm, the concept. The government must change the mindset of the investor, point the investor in the right direction, provide him or her with all the necessary information, for example, about projects in the Far East and in Siberia. We are going to the Far East not to steal resources, but to collaborate in the interests of both parties.

We want to work in the sphere of hydroelectric resources as we think that we can achieve great success quickly in this field. We intend to construct quality hydroelectric power plants in this region that are capable of moving the development of the economy forward and bring economic benefits to the population of the region and to qualitatively improve infrastructure, both of a transport and social nature. People will be pleasantly surprised to see that investments will bring benefits for everybody and they will be won over. I believe that this must be reflected in the attitude of the state and the government towards investors, in the

investment climate, and also in the tax climate as it relates to them. Those are my thoughts.

Thank you.

M. Clifford:

Thank you. As we have mentioned, we have some very special guests in the front row. Doctor Yang mentioned his experiences in Primorsky Krai, particularly in the agricultural area, and so I would like to introduce the Governor of Primorsky Krai, Vladimir Miklushevsky, who perhaps could talk about the agricultural question that Dr. Yang put to him, and also highlight the potential in areas that we have not talked about, such as education in Primorsky Krai. Thank you.

V. Miklushevsky:

I would like to state my agreement with my colleagues who talked about the importance of developing infrastructure, especially transport infrastructure. Primorsky Krai has things to be proud of in this area. In terms of infrastructure development, over the last few years a substantial amount of state investment has gone into Primorsky Krai, including investment from the Federal Budget. This gives us a basis for looking towards the future with optimism.

I would also like to talk about a different sphere of infrastructure, about human capital infrastructure, the infrastructure of education and research. I believe that dynamic and progressive development in the modern economy is impossible without the development of this segment of infrastructure. In this sense, Primorsky Krai is also fortunate: the Far Eastern Federal University was founded, which is a serious point of growth for the economy of Primorsky Krai and the Far East. The strategy for the development of the Federal University assumes the export of educational services, for which we are looking at the Chinese, Indonesian, and Vietnamese markets.

I would like to highlight another very important aspect. I believe that the future of the Far East will be in the development of advanced technologies. The development of

advanced technologies is impossible without education and research, and their close integration. All over the world right now, centres are being founded based in universities, and scientific research circles collaborate with major high-tech corporations. We are moving with this trend: such a centre is being founded within the Far Eastern Federal University, together with the United Shipbuilding Corporation.

There is one more important aspect. In my opinion, it is not always visible on the surface. The population of the Far East is now not very big. It is imperative to solve the problem concerning the prevention of an exodus, and put in place measures to increase the population. Apart from this, we need to create a system for the quick retraining of workers to fulfil current demands. This will allow the job market to react appropriately to the technological changes that are occurring in manufacturing. It is important that the changes in education will be successful, or even be ahead of the changes taking place in industrial manufacturing.

Thank you.

M. Clifford:

Thank you. You mentioned foreign students. Are you actively recruiting students from Indonesia, China, or other parts of East Asia?

V. Miklushevsky:

There is discussion about the Federal University collaborating with leading higher education establishments in the 'Top 100', developing and implementing English-language programmes to be aimed at both foreign and Russian students.

M. Clifford:

I know we have Vadim Shvetsov who is the General Director of Sollers, which is involved in manufacturing – auto manufacturing specifically – in Vladivostok, with SsangYong, Mazda, and soon other Japanese manufacturers. Perhaps you could make a few remarks on manufacturing in that area?

V. Shvetsov:

Mr. Yakunin cited a negative example of working with Japan, whereas I would like to cite a positive example. Over the course of 18 months we created two collaborative enterprises in car manufacturing with Mazda, and with Mitsui we created an additional collaborative enterprise manufacturing Toyota cars. The total production plan of these enterprises came to 100,000 cars. I need to add to these figures the manufacturing output of my company Sollers, where Ssangyong vehicles were produced. The total volume comes to more than 150,000 cars. This is the first example of the creation of a collaborative cluster in the Far East, uniting the efforts of three companies. For us, this is just the first step. It is a commitment which Japanese companies are making to Russia. This would never have happened if we did not demonstrate how it is possible to build car manufacturing capacity in the Far East. I will give you an example. When we began building the factory, investment construction in the Far East cost EUR 2,000 per square metre. When we finished construction it was EUR 1,300, but in Russia this figure was EUR 1,100. This example demonstrates that the Far East presents a big challenge in the sphere of infrastructure. In acknowledging this, it is necessary to work and to make a concerted effort to choose appropriate partners in order to move the situation from a standstill position.

I will underline another aspect of work in Primorsky Krai. I think that Primorsky Krai is the best point of entry into the growing Russian market for Japanese business. Why? Firstly, Japanese companies are now losing their share of the market, even though they had a rather big share, especially in electronics. Secondly, the accepted policy in Japanese circles for the creation of basic production facilities in Japan does not work today. The President of Toyota talked about the two priorities of his company: the hybrid vehicle and its work in fast-growing markets. There is a big opportunity here for knowledge-based industries in the Far East.

I agree with Mr. Miklushevsky, that the future of Vladivostok is in intellect. In Primorsky Krai we need to really create knowledge-based industries. A good

example of the creation of such an industry is Thailand. More than 500 Japanese companies have operations in Thailand. Toyota, Nissan, and Suzuki were also the first to go there, then a few more companies were founded. On the Thai market, around 200 supplier companies materialized, electronics companies came, and then also representatives of other spheres appeared, including logistics operators. Now Thailand not only does work for its internal market, but also for export.

I often hear the suggestion to immediately build export-oriented enterprises. This does not work. At first, a company must show its competitiveness, an ability to work for the domestic market. However, an orientation towards export for these enterprises is a task for the near future.

An important task is the creation of special industrial parks that are an intelligible and familiar model for foreign investors.

Social infrastructure is yet another factor which is very important for foreign investors. For representatives of Japanese companies it is very important where they will live, what they will eat: that is life, and they want to live it without experiencing difficulties.

The main idea that we are suggesting for the Far East is the implementation of industrial clusters. This represents a successful start with a chance to step up automobile manufacturing and vehicle component production. Subsequently, it is imperative to pay attention to electronics and other spheres of industry. I believe that for the Japanese, this is one of the last chances to enter into the fast-growing Russian market.

Thank you.

M. Clifford:

Thank you very much for your interesting thoughts, especially the parallel to Thailand, which is a country of 70 million people, most of whom are fairly close to Bangkok, where the Japanese companies are located. Does the Far East have skills and the number of workers required to adopt the kind of strategy you mentioned?

V. Shvetsov:

Yes, that is one of the big problems. I believe that there is now significant potential in Vladivostok. Currently facilities are being constructed for the APEC 2012 Vladivostok Summit. This construction project alone created many opportunities. If these are not exploited now, they will not be realized. We need to continue the work of APEC and secure those people who came to work on this project. We have the possibility to secure them if we can offer them jobs appropriate to their skills and qualifications.

More fundamental and systemic things will, of course, be built over more time. That includes a good educational system, beginning with comprehensive training, and the resultant good career prospects. It is imperative to develop longer-term programmes. Here, without labour migration, the problem cannot be solved. This must be a systemic, comprehensive task for the Far East, which it must solve.

M. Clifford:

Well, forgive me for being blunt, but it is a long way from the rest of Russia in terms of markets. Where do you sell the cars to? China? Do you sell the cars to the European part of Russia? Where is the market, and is the infrastructure in place to develop it?

V. Shvetsov:

Eighteen months ago, at a press conference in Vladivostok dedicated to the product launch of the Korean brand SsangYong, all of the reporters told me that I would not sell a single car of this brand in Vladivostok. Now we are already have 7% of the market in Vladivostok. Slow and steady wins the race. If you work effectively with the population, it is possible to sell cars. The population of Primorsky Krai has one of the highest concentrations of cars in Russia – most families have two cars, although relatively old ones. The market for vehicle replacement is quite large.

Eastern and Western Siberia are developing at unbelievable speeds from the perspective of consumption. The central part of the region is already not developing as it was before, as the market there is relatively saturated, but in Eastern and Western Siberia and in Vladivostok, consumption is increasing. The market is coming to us. We conducted an assessment with Toyota, with whom we are launching the Prado model. In line with our market research, all Prado models will be sold in Eastern and Western Siberia, up to the Urals. That is why the market is coming to us. This is a promising project, an infrastructural project which will enable us to establish new markets.

M. Clifford:

I believe we have Andrei Slepnev here. You are a member of the Board on Trade for the Eurasian Economic Commission. You have heard what other speakers have said. What comments would you like to add in terms of accelerating the development of Siberia and the Far East?

A. Slepnev:

Thank you very much.

Today is an interesting day. In the first half we discussed the integration dimension at the two plenary sessions, at first in the context of the dialogue between manufacturers and entrepreneurs of Russia and the EU. Then we had the round table discussion on Eurasian integration. In both discussions the question of vectors was raised – the priorities of the Eurasian Union. Should it be to the East, or to the West? Should it be with the EU or with the growing Asian region?

We acknowledge that the formulation of a full network of contacts and cooperation between the Eurasian region and the Asian region is a necessary element of the infrastructure for future collaboration. We know the particularities of working in the Pacific region. This work is based on a network of agreements concerning free trade – that is the actual and current state of affairs. The leaders of three of our countries have already taken a decision to take practical steps towards the formation of a

regime of free trade between countries of the region, not with all countries at once, but following a certain sequence.

In relation to this, a series of interesting observations arise. Firstly, the region has already been functioning for quite a while within an open market regime, and it will be rather complicated for our manufacturers to enter into these markets. The markets are already occupied. First of all, we acknowledge that with the opportunities that there are to make an investment in the development of the region and to implement mutually beneficial projects, questions remain regarding power generation, infrastructure, railways, and aviation technology. It is in these spheres where a high share of government decisions are made regarding which markets supplies will go into. It is imperative that we implement joint projects for the full-scale development of relations between the countries of the region – an important, although not the only part of which, will be an agreement concerning free trade. Concrete agreements determining the balance of interests are also necessary, which will take into account a broad spectrum, including mutual investment, mutual supply, and mutual participation in the development of resources, and so forth.

A certain consensus on the broad approach to entering the region has already been reached. In the near future we will make an announcement about the partner countries with whom we will begin to implement such projects. The preliminary work in this respect is already underway.

I would like to draw your attention again to the very important, necessary element of infrastructure, cooperation, and construction of a fully-fledged dialogue between the two regions. For this it is necessary to express two separate observations about two concrete questions. The question of collaboration in the innovation sphere and in the sphere of technology and development is exceptionally important. Russia is chairing APEC this year and is presenting an initiative that is supported by all countries in the Eurasian economic community. This is an initiative aimed at achieving significant cooperation in the coordination of technical regulations to prevent barriers being set up between regional groupings. This kind of problem really exists today. The European Union is developing and deepening its

regulations. The same work is underway in our unions, and in different structures such as APEC and ASEAN. It is important that new barriers, which could be much more formidable even than barriers between countries themselves, do not arise between integrative unions by virtue of deepening the standards of integration processes. Coordination and cooperation are acquiring a particular importance.

Another area with good prospects, apart from natural resources, are projects in the sphere of agriculture and investment in agricultural production in the Far East. It is a sphere that is capable of having an enormous effect on business, on diversification, on food, and social security in the region.

Thank you.

M. Clifford:

Thank you very much. One area we have not talked about is natural gas. Russia, I think, has the largest natural gas reserves in the world. It is something that I know Hyundai's founder, Chung Ju-Yung, was very keen to develop for an energy poor country like Korea. B.J., what is the outlook for gas?

Bong-Jin Yang:

I confess that I deliberately highlighted the importance of speed. If you look at the market, due to an oversupply of shale gas in the United States, the gas price plummeted to USD 2 per MMBtu. On the other hand, in Japan, it is almost USD 20 per MMBtu, so almost ten times the price as in the United States. So in a sense, the United States has had only inbound energy terminals in the gulf area, but now they are adding outbound energy terminals. So in a sense, you are competing. Russia will end up competing with the United States in supplying gas to East Asia. If you postpone the pipeline construction to South Korea through North Korea, then you will lose the opportunity to sell your PNG. So, I think that it is very clearly important to have speed to grasp the opportunity in your hand.

I think South Korea's imports of coal gas alone are 35 million tonnes of gas per year, and eastern Siberian gas resources should be marketed at very opportune

prices. So, I think you have to speed up to compete for the market in Asia. That would also stabilize the political and diplomatic situation in the Far East as well. So, you have many, many reasons why you have to capitalize on the situation now.

M. Clifford:

How do you think North Korea feels about that pipeline?

Bong-Jin Yang:

Well, they would be more than happy to have that, because that would help Russia, North Korea, and South Korea at the same time. And if you have a pipeline connecting through North Korea, that can end up in the Japanese market, too, because after the Fukushima debacle, Japan gave up nuclear power plants, and they have to increase their thermal power plants by burning gas. So, Russia must grasp the opportunity to market eastern Siberian gas.

M. Clifford:

Oleg Deripaska, if we have this conversation in 10 years, will we still be lamenting how slowly things are going, or do you see the momentum really picking up speed?

O. Deripaska:

I am sure that the situation will be different. We can currently completely value Eastern Siberian GDP and the GDP of the Far East at USD 280–300 billion. We can double this figure in ten years. It is often noted that within 15 years Eastern Siberia and the Far East will become part of the global top 20 in terms of the volume of manufactured goods. Partnership and collaborative programmes of development, infrastructure, and joint programmes to develop certain technologies are very important.

Together with China, we will develop technologies to transfer energy across large distances, using high-voltage lines with alternating as well as direct currents. This will be big progress for us in terms of our relationship with Asia. There will be an

energy bridge, which will link North and South Korea, and Japan. We are sure that on the basis of these technologies, we can connect Siberia with the Urals and with the European part of Russia. We will ensure the optimum use of energy resources across the whole extent of our Eurasian territory.

I believe that the human factor is also important. The inhabitants of the region are expecting changes. In the presentation of our President to Parliament, this was the second issue raised after the issue of demographics. It is important to allocate resources and to establish priorities. It is impossible to do everything at once. At the same time, there are areas where it is already clear that we need to act. In the development process, opportunities will arise for small and medium enterprises, as will those clusters which were talked about earlier. Collaborative enterprises will appear which will create the necessary components for lowering the cost of production. One of our unique advantages is the availability of a competent workforce. We all work in so-called third world countries, in Africa and in Latin America. We understand how hard it is to establish infrastructure and service functions. I would like to say that in any small town in Siberia, you can easily support service functions that require a relatively high level of competence, because the people and the experience are there. We lived like that. It was one of the advantages of the Soviet Union, that almost every enterprise had its own infrastructural basis, which lowered effectiveness from one perspective, but on the other hand, it developed people. Therefore, the potential is there. I am sure that in 10 years we will succeed in implementing this, and in 15 years Siberia will achieve a breakthrough that will allow us to match our neighbouring countries.

M. Clifford:

And how fast can trade grow between China and Russia? It is very small, considering the size of the two economies.

O. Deripaska:

This depends on many factors. There is the resources sector, questions of investment, and questions of product manufacture with complex costs. Resources mean infrastructure. Will we be able to double our export potential within eight years? I think that we can. The question lies in investments and determining priority outputs.

Our priorities must be LNG, gas pipelines, the volume of electrical energy, the quantity of power bridges, and the volume of semi-processed goods manufactured within Russia. The extent to which they are processed is also important.

We must understand we have a common external space with Asia, by which I mean a common habitat. We must take advantage of Siberia's potential. This potential lies in its water resources, but also in the fact that it is a territory that is still in an elemental state, and has real potential for the substantial development of tourism services. These are the lungs of Asia, and the future water source for Asia, without which it already could not continue to survive.

The questions in all of these areas are impossible to solve at the private level alone. The government must coordinate its activity in these areas. Large, natural monopolies must collaborate with each other. For example, Russian Railways and Chinese rail companies could collaborate together, as could RAO UES of Russia and China State; major Russian manufacturers such as EuroSibEnergo, RusHydro, and China Yangtze Power Co.; Russian manufacturers of engineering products and Korean and Chinese companies. We are still discussing business conditions. We must not be rushed. It is necessary to discuss questions of prices, conditions, and about how quickly we can figure things out among each other. While I am sure that in ten years we will succeed in doubling the volume of regional production, I have trouble determining the volume of export. But the potential for development, without a doubt, lies in that area.

Bong-Jin Yang:

As far as numbers are concerned, the trade between Russia and Korea in 1992 was only USD 190 million. It had grown by 2010 to USD 17.6 billion, almost 192 times

the previous number. Last year it was over USD 20 billion. So trade between the two countries is growing dramatically, but direct investment between the two countries is very much in the doldrums. In 1993, only USD 3 million was invested by Korea into Russia. It is still lacking: in 2010 it was only USD 320 million. On the other hand, Russia so far has only invested USD 41 million into South Korea. So even while trade volumes are increasing dramatically, the capital flow between the two countries is non-existent, because of a lack of information and the language barrier, and some other bureaucracies that are very difficult to deal with. So, I think it has to be done in a short space of time.

M. Clifford:

Very interesting. Perhaps Ling Wen or Zhang Cheng, could you comment on the development of trade and the development of investment? Do you think we will see this kind of growth in trade, and do you think we will see more growth in terms of investment?

Ling Wen:

Here we have the numbers for the trade volume between the Far East of Russia and China. Last year, the total trade volumes were USD 8.46 billion, which means 21% growth on the previous year, within which the import from China to the Far East was USD 4.29 billion. The growth rate should be 9.7%. And the output to China was USD 4.17 billion. The growth rate should be 35.6%.

But in total, China should be only the second largest among all of the countries. So we think for Russia, China should be a great potential target country.

Zhang Cheng:

In the future, the development of the Far East will attract increased investment from China in this region, especially direct investment. That will be an absolutely necessary trend.

Thank you.

L. Wen:

I would also like to express one thought. Since Putin took the helm, China and Russia have been talking about many projects, in one year there were 202 projects. Unfortunately, only a few of these were implemented.

I think that if we are not just going to carry on talking about potential collaboration at the Forum, but do something concrete, the best thing would be to give an example of a successful collaboration. I hope that we will work with Mr. Yakunin, with RUSAL, and I hope that this collaboration will be a real one.

Next year, when we participate in the next Forum, we will tell you about the successful projects of our collaboration. We will show you that we have the strength of will to establish such a collaboration.

V. Yakunin:

It seems to me that we are starting to digress a little from the topic of our discussion. We are talking about the problems and opportunities for the development of the Far Eastern economy, and I would like to underline that it is not entirely correct to look at the development of infrastructure from the perspective of transportation of goods and passengers, because the development of infrastructure presents opportunities for a colossal amount of investment projects. Chinese banks are interested in this, South Korean banks are interested in this. I think that we must not forget this opportunity to develop the economy of the Far East and Siberia.

Furthermore, I assume that the development of infrastructure, for example a project for the construction of a railway to the port of Rajin, a Trans-Korean Railway, will radically change the economic situation in this region. Today there are difficulties with developing business partnerships between Russia and South Korea, because for the time being, these can only be established through ports. Port infrastructure is also in need of development. The establishment of a direct network with a Trans-Korean Railway will positively influence the development of the Russian Far East, North Korea, and South Korea.

Of course, the desire of business circles to establish collaboration and the appropriate political support at the level of national governments, which we have just spoken about, are also necessary.

A possible area for collaboration would be the signing of an intergovernmental agreement at an appropriate level, which would ensure a relevant amount of political support for business, so that we could implement our concrete business projects under these documents. Without such support, this will be, to a significant degree, an exercise in theoretical economics.

M. Clifford:

Thank you very much. We have a couple of minutes before we finish. I am told that Alexander Levintal, who is the Deputy of the Presidential Plenipotentiary Envoy to the Far Eastern Federal District, would like to make a remark. Please.

A. Levintal:

Good afternoon.

I have joined this discussion because I think that it is necessary to add some essential points concerning real development of the Far East. It has been said here that trust, political will, and work are needed. I agree with this entirely. These are necessary, but still not sufficient factors for the development of the Russian Far East.

Large spaces, transport underdevelopment, high tariffs for electric energy, transport and so forth: these are the realities of today. People are continuing to leave the Far East. The nominal wage here is higher than the average for Russia, but taking into account power purchasing parity, it is actually lower. The creation of a whole series of particular conditions is required to solve the problems of the Far East, not because it is an economically depressed region, but because Russia, if it wants to be a great power and not miss its opportunity – taking into account the booming development of the Asia-Pacific region – needs a properly developed module, which

will ensure the interconnection of Russia. Entering the Asia-Pacific region is not a task for the Far East, it is a task for Russia.

Therefore, apart from logistics, which is needed, it is necessary to develop a whole series of processing plants. For this, investment is needed. To attract investment, it is imperative to create particular conditions. Unfortunately, nobody has spoken about these particular conditions today. These particular conditions must be created in two areas. First and foremost, they are particular conditions which are different from Russian conditions, both in terms of attracting investment, as well as management conditions. That means different preferences and rules of the game, which would attract private capital here.

You asked whether we are afraid of Chinese investment. No, we are not afraid, because it simply is not present in the Far East. Today it makes up less than 1%. That is the statistic. There is Chinese investment in Moscow, in St. Petersburg, in other regions, but in the Far East there is practically no Chinese investment. Just as there is, unfortunately, no Korean investment. There is the development of major projects, but no investment. Japan only invests in projects around the Sakhalin Shelf. Why? It is obvious that the matter not only has to do with Japanese, Korean, and Chinese decisions, but with the Far Eastern environment, which does not attract these investments. I will cite one last example. Last year, the Russian Far East received RUB 1 trillion out of 10 trillion which was invested in Russia. That is 10% of investment in Russia. That is an excellent indicator as the population share of the region was 4.4% of the population of Russia. But if we do not look at APEC, the construction of gas pipelines, or oil pipelines, a very small share goes into private investment. That leads to the question of particular conditions. Today we have the political will: for the first time in the history of the country, a Ministry has been organized for the development of the Far East. It is imperative to create a law on the development of the Far East and Eastern Siberia with particular conditions. Only in this circumstance will we be able to come and say that the problem has begun to be solved. If this does not happen, without particular conditions there will be no willingness either to retain the population or to attract private investment,.

That is what I would like to include in the discussion.

M. Clifford:

Good. I think that is an excellent and very optimistic and realistic way of ending what I hope you will agree has been a very, very interesting session. I think if I could summarize in just a few words: the political will is there, at least in Russia. Business plays a very, very important role in building trust between these very important neighbouring countries. We need speed, we need investment, we need people, and we just need to get on with the job. So, I hope that next time we come back we will have made a lot of progress.

Thank you, all, you have been a great panel. Thank you.